SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No. 271

IN THE MATTER OF 620 CHURCH STREET BUILDING CORPORATION ET AL., PETITIONERS

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., OCTOBER 19, 1936.

—8306-C

At a regular term of the United States Court of Appeals for the Seventh Circuit begun and held in the United States Court Room in the city of Chicago in said Seventh Circuit on the first day of October, 1935, of the October Term in the year of our Lord one thousand nine hundred and thirty-five and of our Independence the one hundred and forty-fifth.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.
620 Church Street Building Corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby, Emil Rosenthal and B. K. Goodman,
Petitioners.

Petition for leave to appeal from an Order of the District Court of the United States for the Northern District of Illinois, Eastern Division.

And on, to wit: On the twenty-fifth day of April, 1936, there was filed in the office of the Clerk of this Court a Notice and Proof of Service, which said Notice and Proof of Service is in the words and figures following, to wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

5869.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

Petition for appeal from order of confirmation entered in proceedings for corporate reorganization under Section 77B of the Bankruptcy Act, as amended, in Case No. 56,564, in the District Court of the United States, Northern District of Illinois, Eastern Division.

Honorable
John P. Barnes,
Judge Presiding.

NOTICE.

To Defrees, Buckingham, Jones & Hoffman, 38 S. Dearborn Street,

George W. Swain, 134 S. LaSalle Street, Chicago.

Gotthard A. Dahlberg, 11 S. LaSalle Street, Chicago.

Pam & Hurd, 231 South LaSalle Street, Chicago.

Wilhartz, Hirsch & Schanfarber, 38 S. Dearborn St., Chicago.

Sonnenschein, Berkson, Lautmann, Levinson & Morse, 77 West Washington Street, Chicago, Illinois.

You Are Hereby Notified that on Saturday, April 25, 1936, we shall file with the Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, the petition of 620 Church Street Building Corporation, Irene K. Goodman, G. Walter, M. Long, A. W. Kibby, Emil Rosenthal and B. K. Goodman, for leave to appeal from that certain order of confirmation of the District Court of the United States, for the Northern District of Illinois, Eastern Division, entered on March 31, A. D. 1936, in the proceedings therein pending entitled "In the matter of 620 Church Street Building Corporation, a corporation, Debtor", Case No. 56564, and we shall also file

therewith the joint assignment of errors of petitioners and brief in support of petition for leave to appeal.

ISAAC M. MILLS,
THEODORE E. REIN,
MORTON C. CHESLER,
IRVING L. BLOCK,
Chicago, Illinois,
Counsel for Petitioners.

Received a copy of the above and foregoing notice, and copy of the petition, assignment of errors and brief therein mentioned, this 25th day of April, A. D. 1936.

SCOTT, MACLEISH & FALK,
GEO. W. SWAIN,
PAM & HURD,
WILHARTZ, HIRSCH & SCHANFARBER,
DEFREES, BUCKINGHAM, JONES & HOFFMAN,
GOTTHARD A. DAHLBERG, H. D.
SONNENSCHEIN, BERKSON, LAUTMANN, LEVINSON & MORSE.

Endorsed: Filed Apr. 25, 1936, Frederick G. Campbell, Clerk.

And on the same day, to wit: On the twenty-fifth day of April, 1936, there was filed in the office of the Clerk of this Court a Petition for Leave to Appeal, which said Petition for Leave to Appeal is in the words and figures following, to wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5869.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

Petition for appeal from order of confirmation entered in proceedings for corporate reorganization under Section 77B of the Bankruptcy Act, as amended, in Case No. 56,564, in the District Court of the United States, Northern District of Illinois, Eastern Division.

Honorable
John P. Barnes,
Judge Presiding.

PETITION FOR LEAVE TO APPEAL.

To the Honorable Judges of the United States Circuit Court of Appeals, for the Seventh Circuit:

Your petitioners, 620 Church Street Building Corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby, Emil Rosenthal and B. K. Goodman, respectively pray for leave to appeal from the order of confirmation of the United States District Court for the Northern District of Illinois, Eastern Division thereof, made by the Honorable John P. Barnes, one of the Judges thereof, on the 31st day of March, 1936, depriving these petitioners of their property without due process of law and in violation of the Constitution of the United States of America.

Respective Interests of Petitioners.

Your petitioner, 620 Church Street Building Corporation, respectfully represents that it is the debtor herein and is the owner of all of the assets described in its petition and herein sought to be affected.

Your petitioners, Irene Goodman, G. Walter, M. Long and A. W. Kibby, respectfully represent that they are the legal owners and holders of all of the issued and outstanding capi-

tal stock of the said 620 Church Street Building Corporation, debtor, holding, respectively, twelve hundred sixty-seven (1267), one (1), one (1) and one (1) shares of said capital stock, and more particularly described in the verified proofs of claim heretofore filed and allowed in the court below.

Your petitioner, Emil Rosenthal, respectfully represents that he is the legal owner and holder of all of the outstanding and unpaid principal second mortgage notes in the principal amount of $40,250.00 with interest thereon since December 13, 1929, which notes are secured by trust deed dated July 13, 1928, from the Carlson Annex Building Corporation to B. K. Goodman, as trustee, conveying the real estate involved in the court below and more particularly described in the verified proof of claim heretofore filed and allowed in the court below.

Your petitioner, B. K. Goodman, respectfully represents that he is the legal owner and holder of the sole outstanding and unpaid principal third mortgage note in the sum of $27,000.00 with interest thereon since December 3, 1931, which note is secured by trust deed dated June 3, 1931, made by the 620 Church Street Building Corporation to W. Kahn, as trustee, conveying the real estate involved in the court below and more particularly described in the verified proof of claim heretofore filed and allowed in the court below.

Summary of the Facts.

Your petitioners respectfully represent that the following is a summary statement of the facts upon which the order of confirmation complained of has been entered, creating important and fundamental questions involving the substantive property rights of petitioners under Section 77B of the Bankruptcy Act, as amended, to-wit:

1. That your petitioner, 620 Church Street Building Corporation (herein in the proceedings below referred to as "Debtor"), is at the present time, and has been since the date of its incorporation, engaged in the business of acquiring and owning one building, and the site therefor, consisting of the premises commonly known as 620 Church Street, Evanston, Illinois. The principal asset of the debtor consists of the real estate described as follows:

> Leasehold estates for a term ending August 31, 2021, in Sub-lots 1 and 2 of Lots 2 and 3 in Block 19 original

Village (now City) of Evanston, Illinois, excepting the South 15 feet of said Sub-lots 1 and 2, dedicated for use as public alley and together with the vacated alley lying West of and adjacent to said Sub-lot 2, said leaseholds having been created by Indentures of Lease between Northwestern University and Victor C. Carlson and Charlotte Carlson, one dated July 27, 1922, and the other dated April 20, 1928, as amended by an Agreement between Lessor and Lessees dated June 20, 1928.

2. That the improvements upon said leasehold estate consist of a part seven-story and part two-story and basement store, merchandise and office building of fire proof construction.

3. That the present capitalization of the said debtor is as follows:

(a) First Mortgage Six Per Cent Building and Leasehold Serial Gold Bonds (Carlson Annex Bonds) issued by Carlson Annex Building Corporation, predecessor of 620 Corporation, and secured by a trust deed dated June 30, 1928, to The Bank of America and Edgar N. Greenbaum, as trustees, and recorded in the Office of the Recorder of Deeds of Cook County, Illinois, as Document No. 10085077.

Principal amount outstanding.....$445,500
with appurtenant interest coupons maturing July 1, 1931, and thereafter.

NOTE: Proceedings were heretofore commenced in the Circuit Court of Cook County, Illinois, to foreclose the lien of trust deed securing the Carlson Annex Bonds in a cause entitled *Louis M. Quitman, etc. as Successor Trustee* v. *Carlson Annex Building Corporation, et al.,* in the Circuit Court of Cook County, Illinois, No. B-223577.

(b) Notes (herein sometimes called "Second Mortgage Notes") secured by a trust deed dated July 13, 1928, from Carlson Annex Building Corporation to B. K. Goodman, as Trustee, recorded on July 25, 1928, in the Recorder's Office of Cook County, Illinois, as Document No. 10099385.

Principal amount outstanding..... $40,250
together with interest thereon since December 13, 1929.

(c) Note (herein sometimes called "Third Mortgage Note") secured by a trust deed dated June 3, 1931,

from 620 Corporation to W. Kahn, as Trustee, recorded on June 5, 1931, in the Recorder's Office of Cook County, Illinois, as Document No. 10915337.

Principal amount outstanding..... $27,000
together with interest thereon since December 3, 1931.

(d) Common stock of no par value..... 1260 shares.

4. That claims upon all of the above obligations have been filed and allowed in the proceedings below; that all of said obligations described in subdivisions (b), (c) and (d) of the preceding paragraph of this petition, are owned and held entirely by your petitioners herein.

5. That on July 12, 1934, the debtor (one of your petitioners herein) filed its voluntary petition for reorganization under Section 77B of the Bankruptcy Act as amended, in the District Court of the United States for the Northern District of Illinois, Eastern Division thereof, in proceedings bearing No. 56,564; that subsequently, on the 5th day of November, 1934, Warner G. Baird was appointed permanent trustee of the debtor's property; that said Warner G. Baird is now the duly qualified and acting trustee of the debtor's property in the proceedings herein.

6. That Chester R. Davis, Murray Wolbach and James B. McCahey, acting as a committee for the First Mortgage Six Percent Building and Leasehold Serial Gold Bonds issued by the Carlson Annex Building corporation (referred to in these proceedings as the "Protective Committee") intervened in the proceedings below for and on behalf of the bondholders who deposited bonds with said committee.

7. That from the time of the institution of the proceedings below, your petitioners conferred and negotiated with the said protective committee for the purpose of creating and consenting to a fair and feasible plan of reorganization of the debtor's assets and liabilities.

8. That notwithstanding your petitioners' desire to cooperate to the end that such a plan of reorganization be consummated, the said protective committee, on or about the 30th day of January, 1936, pursuant to leave of court, filed their plan of reorganization (herein referred to as "Plan") purporting to effect a reorganization of the debtor's property.

9. That said plan provides, in brief, that the property of the debtor be reorganized together with the adjacent building known as the 636 Church Street Building Corporation (by whom a petition was likewise filed for reorganization

under Section 77B of the Bankruptcy Act, in the District Court below, in a case therein pending bearing No. 56187), through the medium of a new corporation which, under the said plan, is to acquire all of the assets of both building corporations; that the said plan provides that a certain pro rata portion of the securities of the new corporation are to be distributed to the holders of the indebtedness against the 636 Church Street Building Corporation and to the holders of the bonds secured by the present first mortgage on the 620 Church Street Building Corporation, debtor herein, thus failing to make provision for payment of any kind whatsoever to the holders of the second mortgage in the sum of $40,250.00, and to the holders of the third mortgage in the sum of $27,000.00 presently existing on the property of the debtor, 620 Church Street Building Corporation (being the entire Class 3 and entire Class 4 of claims against the debtor's property); that said plan does not provide for any consideration or distribution to the holders of the capital stock of the 620 Church Street Building Corporation, debtor (being the entire Class 5 of claims against the debtor's property).

10. That pursuant to leave granted by the District Court below, your petitioners filed objections to said plan which, in substance, were based upon the fact that the said plan did not provide adequate protection for the realization by the holders of the second mortgage notes and the holder of the third mortgage note and of the holders of the capital stock of the debtor of the value of their liens and claims against the debtor's property, and that said plan was unfair and inequitable and contrary to the Constitution of the United States of America, in that said plan was repugnant to the Fifth Amendment of the Constitution.

11. That pursuant to the suggestion and request of the District Court below, various appraisals of the debtor's property were submitted to said court, which appraisals varied from the sum of $205,000.00 to $600,000.00.

12. That the said protective committee, acting under the said deposit agreement on behalf of the holders of $371,300 principal amount of said first mortgage bonds, being an amount in excess of sixty-six and two-thirds in amount of the aggregate amount of allowed claims of Class 2 (being that class concerning claims based upon said first mortgage bonds), consented to and accepted the said plan so filed by said committee.

13. That no acceptance by any claimant in either Class 3

(being that class concerning claims based upon the said second mortgage notes) or Class 4 (being that class concerning claims based upon the said third mortgage note) or Class 5 (being that class concerning claims based upon the capital stock of the debtor) was filed with respect to said plan which was confirmed by the order of the District Court below, and of which your petitioners now make complaint.

14. That subsequently, on the 31st day of March, 1936, the District Court below entered an order of confirmation (from which this appeal is sought, a copy of which order is attached to this petition as Exhibit "A"), finding, among other things, that the leasehold estate of the debtor has a fair market value of $245,025.00 and that there is no equity in said estate over and above the $445,500.00 of principal amount of first mortgage bonds and that the debtor is accordingly insolvent, and that the consent of a majority of the stockholders of the debtor is not a prerequisite to the confirmation of the plan; that said order, in paragraph 12 thereof, purported to appraise all claims filed in Class 3 (the second mortgage notes) and all claims filed in Class 4 (the third mortgage note) to be of no value, and that therefore the consent of sixty-six and two-thirds in amount of claims allowed in said Class 3 and the consent of sixty-six and two-thirds in amount of claims in said Class 4 were not a prerequisite to the confirmation of the said plan.

15. That your petitioners refer to the Assignment of Errors filed by them simultaneously with this petition, setting forth the errors made by the District Court below, and giving the grounds for this appeal, and hereby make said Assignment of Errors a part hereof.

Wherefore, your petitioners pray that they may be allowed, in the discretion of this Honorable Court, to appeal in matter of law herein, and that the prayer of said petition be granted and a citation be issued directed to Warner G. Baird, trustee of debtor, Chester R. Davis, Murray Wolbach and James B. McCahey, acting as a committee for the holders of First Mortgage Six Percent Building and Leasehold Serial Gold Bonds issued by Carlson Annex Building Corporation, under the terms of a deposit agreement dated December 12, 1929 (referred to in these proceedings as the "Committee"), Louis M. Quitman and Edgar N. Greenebaum, as trustees under trust deed dated June 30, 1928, made by Carlson Annex Building Corporation, William L. O'Connell, as receiver of the Central Republic Trust Company, and of Central Repub-

lic Trust Company as Trustee by succession through consolidation, Clara Abt, Lucille Abt, Edward Schoen and Alice G. Hirsh, commanding them to appear before the said United States Circuit Court of Appeals, for the Seventh Circuit, to do and receive what may appertain to justice to be done in the premises, and that a transcript of the record and proceedings in said proceeding, duly authenticated, may be transmitted to the United States Circuit Court of Appeals for the Seventh Circuit.

And your petitioners will ever pray.

620 CHURCH STREET BUILDING CORPORATION,
By G. WALTER,
Its Vice President.

IRENE GOODMAN,
G. WALTER,
M. LONG and
A. W. KIBBY,
By G. WALTER,
Their duly authorized agent.

B. K. GOODMAN,
EMIL ROSENTHAL.

State of Illinois } ss.
County of Cook }

G. WALTER, being first duly sworn, on oath deposes and says that she is the Vice President of the 620 Church Street Building Corporation, petitioner herein; that she has read the foregoing petition by her subscribed, knows the contents thereof and that the same is true in substance and in fact.

G. WALTER.

Subscribed and Sworn to before me this 24 day of April, 1936.

MORTON CHESTER,
Notary Public.

(Notarial Seal)

State of Illinois } ss.
County of Cook }

G. WALTER, being first duly sworn, on oath deposes and says that she is one of the petitioners herein and is the duly authorized agent of G. Walter, M. Long, and A. W. Kibby,

petitioners; that she has read the foregoing petition by her subscribed, knows the contents thereof and that the same is true in substance and in fact.

G. WALTER.

Subscribed and Sworn to before me this 24th day of April, 1936.

(Notarial Seal)

MORTON CHESTER,
Notary Public.

State of Illinois } ss.
County of Cook }

EMIL ROSENTHAL, being first duly sworn, on oath deposes and says that he is one of the petitioners herein; that he has read the foregoing petition by him subscribed, knows the contents thereof and that the same is true in substance and in fact.

EMIL ROSENTHAL.

Subscribed and Sworn to before me this 24 day of April, 1936.

(Notarial Seal)

MORTON CHESTER,
Notary Public.

State of Illinois } ss.
County of Cook }

B. K. GOODMAN, being first duly sworn, on oath deposes and says that he is one of the petitioners herein; that he has read the foregoing petition by him subscribed, knows the contents thereof and that the same is true in substance and in fact.

B. K. GOODMAN.

Subscribed and Sworn to before me this 24 day of April, 1936.

(Notarial Seal)

MORTON CHESTER,
Notary Public.

IN THE DISTRICT COURT OF THE UNITED STATES

For the Northern District of Illinois,

Eastern Division.

In the Matter of
620 Church Street Building Corporation,
a corporation,
Debtor. } No. 56564.

ORDER OF CONFIRMATION.

This cause coming on for hearing pursuant to order entered herein on the 30th day of January, 1936, for the proposal, consideration, and confirmation of the Plan of Reorganization dated as of January 30, 1936 (hereinafter sometimes referred to as the "Plan"), filed in this proceeding on January 30, 1936, by Chester R. Davis, Murray Wolbach, and Charles B. McCahey, acting as a Committee for the holders of First Mortgage Six Per Cent Building and Leasehold Serial Gold Bonds (hereinafter sometimes called "Carlson Annex Bonds"), issued by Carlson Annex Building Corporation and secured by trust deed dated June 30, 1928, to The Bank of America and Edgar N. Greenebaum, as Trustees, under the terms of a Deposit Agreement dated December 12, 1929, as amended (hereinafter sometimes referred to as the "Committee"), and upon other matters set forth in said order of January 30, 1936, and for the determination of such other matters as may be properly before the Court, and the Court having examined the Plan and having heard the statements and arguments of counsel, and having considered the objections filed to the Plan, and being fully advised in the premises, Finds, Orders, Adjudges and Decrees:

1. That the petition for reorganization heretofore filed herein has been approved as properly filed and filed in good faith, and that the Court has jurisdiction in this proceeding of said Debtor and of all its creditors and stockholders and all of the parties in interest in the reorganization of said Debtor and has jurisdiction of the property of the Debtor and of the subject matter of this cause.

2. Notice of the hearing on the Plan of Reorganization and the objections thereto and of the other matters set forth

in the order of this Court entered herein on January 30, 1936, has been duly given to the creditors and stockholders of the Debtor and claimants against its property and assets and to all other parties in interest as is required by said order and notice of the submission of this order has been given to all counsel of record.

3. That for the purposes of any plan of reorganization proposed in this proceeding and its acceptance, the Court divided the creditors and stockholders of Debtor into six classes according to the nature of their respective claims and interests, namely:

Class 1: Those claims allowed in these proceedings against 620 Church Street Building Corporation, or its property, entitled to priority under Section 77B of the Bankruptcy Act as amended.

Class 2: Those claims allowed in these proceedings against 620 Church Street Building Corporation, or its property, with respect to the First Mortgage Six Per Cent Building and Leasehold Serial Gold Bonds issued by Carlson Annex Building Corporation under trust deed dated June 30, 1928, from Carlson Annex Building Corporation to The Bank of America and Edgar N. Greenebaum, as trustees.

Class 3: Those claims allowed in these proceedings against 620 Church Street Building Corporation, or its property, with respect to the Notes secured by trust deed dated July 13, 1928, from Carlson Annex Building Corporation to B. K. Goodman, as trustee.

Class 4: Those claims allowed in these proceedings against 620 Church Street Building Corporation, or its property, with respect to the note secured by trust deed dated June 3, 1931, from 620 Church Street Building Corporation to W. Kahn, as trustee.

Class 5: Those interests of stockholders allowed in these proceedings in 620 Church Street Building Corporation with respect to the shares of capital stock of 620 Church Street Building Corporation.

Class 6: Those claims and interests allowed in these proceedings against and in 620 Church Street Building Corporation, or its property, represented by claims or interests of whatever character other than as above in the foregoing classes 1 to 5, inclusive, enumerated against 620 Church Street Building Corporation, or its property, whether or not the same be evidenced by written instrument.

4. That the time of filing or the manner of proving or

evidencing claims in Class 1 has not yet been fixed, provision being made hereinafter in this order for such filing and approving or evidencing, to the extent necessary or advisable, unless hereafter otherwise determined advisable by the Court. The Plan provides that all costs of administration and other allowances made and approved by the Court in the proceedings for the reorganization of the Debtor are to be paid in cash in full by the Debtor, and, therefore, such claims are not affected by the Plan, and the acceptance of the Plan by the holders of such claims is not a prerequisite to the confirmation of the Plan.

5. That the Committee acting under the Deposit Agreement dated December 12, 1929, referred to above, is lawfully constituted, and that the said Committee has full power, right and authority to consent to and accept the Plan for and on behalf of each of the holders of Carlson Annex Bonds deposited with said Committee under said Deposit Agreement; that the Committee has accepted the Plan in writing on behalf of the holders of all Carlson Annex Bonds on deposit with it under said Deposit Agreement, to-wit: on behalf of the holders of $371,300 principal amount of said Bonds with interest thereon, which amount is in excess of 66 2/3% of the aggregate amount of allowed claims of Class 2, and such consent and acceptance so filed by the Committee is hereby declared to constitute the consent and acceptance of the Plan by the holders of the Certificates of Deposit issued under said Deposit Agreement in respect of said Carlson Annex Bonds on deposit with the Committee thereunder.

6. That for the reasons hereinafter set forth, the acceptance of the Plan by the holders of allowed claims in Class 3 is not a prerequisite for the confirmation of the Plan.

7. That for the reasons hereinafter set forth, the acceptance of the Plan by the holder of the allowed claim in Class 4 is not a prerequisite for the confirmation of the Plan.

8. That for the reasons hereinafter set forth, the acceptance of the Plan by the stockholders of the Debtor is not a prerequisite for the confirmation of the Plan.

9. That no claim has been filed in Class 6.

10. That a reasonable time has been determined and fixed within which the claims and interests of creditors and stockholders might be filed or evidenced, and said time having expired no claim or interest not heretofore filed or evidenced herein and allowed may participate in the Plan except on order for cause shown.

11. That the Court having heard evidence and testimony on the value of the property of the Debtor finds: that the principal property of the Debtor consists of the two leasehold estates and improvements on the property located at 620 to 628 Church Street, in the City of Evanston, County of Cook, and State of Illinois, said two leasehold estates, together with all improvements thereon and appurtenances thereto, being more specifically described in the Plan and being hereinafter sometimes referred to as the "Carlson Building Annex"; that the Carlson Building Annex has a fair market value of $245,025, and that there is no equity over and above the $445,500 principal amount of Carlson Annex Bonds outstanding against the Carlson Building Annex; that the Debtor is accordingly insolvent; that the stockholders are not entitled to participate in the Plan, and that their acceptance of the Plan is not a prerequisite to the confirmation of the Plan.

12. That based on the abovementioned evidence and testimony concerning the value of the Carlson Building Annex, the Court has appraised and does hereby appraise all claims allowed in Class 3 and Class 4 to be of no value, there being no equity in the Carlson Building Annex Bonds outstanding against the Carlson Building Annex, and accordingly no securities, cash or any other thing of value shall be distributed under the plan in respect of any of the claims allowed in Classes 3 and 4, and the acceptance of the Plan by the holders of such claims is not a prerequisite to the confirmation of the Plan. The Court further finds that the foregoing method of treatment of the holders of claims in Classes 3 and 4 provides adequate protection for the realization by the holders thereof of the value thereof under and consistent with the circumstances of the case, the same being of no value.

13. That the Plan has been accepted as required by the provisions of subdivision (e) of Section 77B of the Act to Establish a Uniform System of Bankruptcy throughout the United States as amended (hereinafter referred to as the "Bankruptcy Act"), and the above described acceptances have been filed in this proceeding.

14. That by reason of the number of securities of the Debtor outstanding and the extent of the public dealing therein the preparation of a verified statement showing what claims and shares of stock have been purchased or transferred by those accepting the Plan after the commencement or in contemplation of this proceeding, and the circumstances of such purchase or transfer, would be impractical, and, therefore,

the Court directs that such statement need not be filed in this proceeding.

15. That the Plan is fair, equitable, and feasible, and does not discriminate unfairly in favor of any class or classes of creditors or stockholders.

16. That the Plan complies with the provisions of subdivision (b) of Section 77B of the Bankruptcy Act.

17. That the offer of the Plan and its acceptance are in good faith, and were not made or procured by any means or promises forbidden by the Bankruptcy Act.

18. That all amounts to be paid by the Debtor and all amounts to be paid to committees or reorganization managers for services or expenses incident to the reorganization have been approved by or shall be subject to the approval of the judge of this court to whom this cause is assigned or of such other judge of this court as may be hearing this cause.

19. That the Debtor is not a utility subject to the jurisdiction of a regulatory commission or other regulatory authority created by the laws of the State of Illinois.

20. That all provisions of the Bankruptcy Act which ought to be complied with prior to the confirmation of the Plan have been fully complied with in the manner provided therein.

21. That all objections to the Plan, oral or written, are hereby overruled, and the Plan is hereby in all respects finally approved and confirmed.

22. That the provisions of the Plan and of this order shall be binding upon the Debtor, all of its stockholders, including those who have not as well as those who have accepted the Plan, and all creditors of the Debtor, secured or unsecured, whether or not affected by the Plan, and whether or not their claims have been filed, and if filed whether or not allowed, including creditors who have not as well as those who have accepted the Plan.

23. That Warner G. Baird, Trustee of the Debtor, and the above mentioned Committee, shall have full power and authority to, and shall, put into effect and carry out the Plan and orders of the Judge relative thereto, under and subject to the supervision and control of the Judge, and that the said Trustee and Committee shall report to this Court on April 30, 1936, as to the matters and things done and steps taken by them in connection with consummating the Plan as herein confirmed.

24. All petitions seeking the allowance of compensation for services rendered and reimbursement for actual and neces-

sary expenses incurred in connection with this proceeding and the Plan, by officers, parties in interest, depositaries, committees or other representatives of creditors and stockholders of the Debtor and the attorneys or agents of any of the foregoing and of the Debtor and for payment of administrative expenses and allowances in connection with the foreclosure proceedings in the Circuit Court of Cook County, Illinois, in cause No. B-223577, shall be filed with the Clerk of this Court on or before April 20, 1936.

25. This cause be, and hereby is, continued to April 30, 1936, at 10:00 A. M., for the consideration by the Court of said report of the Trustee and the Committee and of petitions for fees, expenses and allowances, and the determination thereof, and for the consideration and determination of all matters germane to this proceeding not hereby or heretofore determined in this matter and the entry of such further order or orders in connection therewith, and in the interim, the right is hereby granted to the Committee and any other persons in interest to apply to this Court for further direction and instructions in respect of any of the matters covered by this order and by the Plan, and the Court hereby reserves jurisdiction to hear and determine the subject matter of any such application and for the entry of such further order or orders and of a final decree in this proceeding.

To all of which the Debtor, 620 Church Street Building Corporation, and its stockholders, Irene Goodman, G. Walter, M. Long and A. W. Kibby, claimants under Class 5 (Claim No. 11), and Emil Rosenthal, claimant under Class 3 (Claim No. 9) and B. K. Goodman, claimant under Class 4 (Claim No. 11), object and except.

BARNES,
Judge.

Dated: March 31, 1936.

Endorsed: Filed Apr. 25, 1936, Frederick G. Campbell, Clerk.

And on the same day, to wit: On the twenty-fifth day of April, 1936, there was filed in the office of the Clerk of this Court an Assignment of Errors, which said Assignment of Errors is in the words and figures following, to wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5869.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

Assignment of errors in support of petition for appeal from order of confirmation entered in proceedings for corporate reorganization under Section 77B of the Bankruptcy Act, as amended, in Case No. 56564, in the District Court of the United States, for the Northern District of Illinois, Eastern Division.

Honorable
John P. Barnes,
Judge Presiding.

JOINT ASSIGNMENT OF ERRORS FILED ON BEHALF OF 620 CHURCH STREET BUILDING CORPORATION, IRENE GOODMAN, G. WALTER, M. LONG, A. W. KIBBY, B. K. GOODMAN, AND EMIL ROSENTHAL, APPELLANTS.

Now come 620 Church Street Building Corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby, and B. K. Goodman, by Sabath, Perlman, Goodman & Rein, their attorneys, and Emil Rosenthal, by Irving L. Block, his attorney, (Petitioners) appellants, and file this, their Assignment of Errors, complaining as follows:

1. That the District Court erred in finding and decreeing that the acceptance of the plan described in said order of March 31, 1936, by the holders of allowed claims in Class 3 (being those claims allowed against the debtor or its property with respect to the second mortgage notes) was not a prerequisite for the confirmation of the said plan.

2. That the District Court erred in finding and decreeing that the acceptance of the plan described in said order of March 31, 1936, by the holders of allowed claims in Class 4 (being those claims allowed against the debtor or its property with respect to the third mortgage note) was not a prerequisite for the confirmation of the said plan.

3. That the District Court erred in finding and decreeing that the acceptance of the plan described in said order of March 31, 1936, by the stockholders of the debtor was not a prerequisite for the confirmation of the said plan.

4. That the District Court erred in finding and decreeing that the fair cash market value of debtor's property is the sum of $245,025.00, and further erred in finding and decreeing tha tthere is no equity over and above the principal amount of Carlson Annex bonds outstanding against the property of the debtor, and further erred in finding and decreeing that the debtor was insolvent, and further erred in finding and decreeing that the stockholders of said debtor are not entitled to participate in the said plan and that their acceptance of the plan is not a prerequisite to the confirmation of said plan.

5. That the District Court erred in finding and decreeing that no securities, cash or any other thing of value should be distributed under the plan in respect of any of the claims allowed in said Classes 3 and 4.

6. That the District Court erred in finding and decreeing that the method of treatment of the holders of claims in said Classes 3 and 4 provides adequate protection for the realization by the holders thereof of the value thereof under and consistent with the circumstances of the case.

7. That the District Court erred in appraising and finding that all claims allowed in said Class 3 and Class 4 are of no value.

8. That the District Court erred in finding and decreeing that the plan has been accepted as required by the provisions of Subdivision E of Section 77B of the Bankruptcy Act.

9. That the District Court erred in finding and decreeing that said plan is fair, equitable and feasible, and does not discriminate unfairly in favor of any class or classes of creditors or stockholders.

10. That the District Court erred in finding and decreeing that the said plan complies with the provisions of Subdivision B of Section 77B of the Bankruptcy Act.

11. That the District Court erred in finding and decreeing that all provisions of the Bankruptcy Act which ought to be complied with prior to the confirmation of the plan have been fully complied with in the manner provided therein.

12. That the District Court erred in finding and decreeing that all objections to the said plan, oral or written, be overruled, and that the said plan be in all respects finally approved and confirmed.

13. That the District Court erred in overruling the objections of 620 Church Street Building Corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby, Emil Rosenthal and B. K. Goodman.

14. That the District Court erred in not finding and decreeing that said plan does not provide adequate protection for the realization by the holders of claims allowed in said Classes 3 and 4 and by the stockholders of the debtor of the value of their respective claims in and to the assets of the debtor.

15. That the District Court erred in not finding and decreeing that said plan discriminates unfairly in favor of the first mortgage bondholders and against the stockholders of the debtor and against the holders of allowed claims in said Classes 3 and 4.

16. That the District Court erred in not finding and decreeing that said plan of reorganization is unfair, inequitable and contrary to the Constitution of the United States of America, in that said plan and the order of confirmation thereof are repugnant to the Fifth Amendment of said Constitution.

17. That the District Court erred in finding and decreeing that the provisions of said plan and said order of confirmation shall be binding upon the debtor, or its stockholders, including those who have not, as well as those who have, accepted the said plan, and all creditors of the debtor, secured or unsecured, whether or not affected by said plan, and whether their claims have been filed, and if filed or not, allowed, including creditors who have not, as well as those who have, accepted the plan.

Respectfully submitted,
620 CHURCH STREET BUILDING CORPORATION,
IRENE GOODMAN, G. WALTER, M. LONG,
A. W. KIBBY, and B. K. GOODMAN,
By ISAAC M. MILLS,
THEODORE E. REIN,
MORTON C. CHESLER,
Their Attorneys.

EMIL ROSENTHAL,
By IRVING L. BLOCK,
His Attorney.

Endorsed: Filed Apr. 25, 1936. Frederick G. Campbell, Clerk.

And afterwards, to wit: On the eleventh day of May, 1936, there was filed in the office of the Clerk of this Court a Memorandum of the Court on Petition for Leave to Appeal, which said Memorandum of the Court is in the words and figures following, to wit: Filed May 1936.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5869.

In the Matter of
620 Church Street Building Corporation, a Corporation,
Debtor.

MEMORANDUM ON PETITION FOR APPEAL.

Petitioners are a debtor, the owners of all of its capital stock, and the holders of all the notes secured by a second and third mortgage on the debtor's premises. They seek to appeal from an order of confirmation of a plan to which they filed objections in the proceedings under section 77B. The plan was confirmed over their objections on the ground that the value of the property was less than the amount of the first mortgage, hence they were not adversely affected by it. Appraisals were submitted to the court which varied from $205,000 to $600,000, and the court found the fair market value of the premises to be $245,125, and that there was no equity in the estate over and above the $445,500 of principal amount due on the first mortgage bonds, and that the debtor was insolvent, and the consent of the majority of the stockholders was not prerequisite to the confirmation of the plan.

The court did not err in ruling that if the property were not worth the amount of the first mortgage indebtedness, the junior interests had no equity to be protected. In view of the fact that, upon what must have been a full hearing as to value of the premises, the court made a specific finding as to that value, this court would have no right to disturb that finding. If there is no equity left, these interests have no right to challenge the plan approved by those parties who are materially interested. Section 77B, subsection (e) provides

that acceptance is not requisite to the confirmation of the plan by any stockholder or class of stockholders if the judge shall have determined that the debtor is insolvent, as he did in this case.

Appeal

DENIED.

Endorsed: Filed May 11, 1936. Frederick G. Campbell, Clerk.

And on the same day, to wit: On the eleventh day of May, 1936, the following further proceedings were had and entered of record, to wit:

Monday, May 11, 1936.

Court met pursuant to adjournment.

Before:

Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.
Hon. Samuel Alschuler, Circuit Judge.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

620 Church Street Building Corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby, Emil Rosenthal, and B. K. Goodman.

Petition for leave to appeal from an Order of the District Court of the United States for the Northern District of Illinois, Eastern Division.

It is now here ordered, adjudged and decreed by this Court that the petition of 620 Church Street Building Corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby, Emil Rosenthal and B. K. Goodman for leave to appeal from the Order or Decree of the District Court of the United States for the Northern District of Illinois, Eastern Division, entered therein on March 31, 1936 In The Matter Of 620 Church Street Building Corporation, a corporation, Debtor, be, and the same is hereby denied.

And afterwards, to wit: On the ninth day of June, 1936, there was filed in the office of the Clerk of this Court a Motion to Vacate Order Denying Leave to Appeal, which said Motion is in the words and figures following, to wit:

No. 5869.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

MOTION OF PETITIONERS TO VACATE ORDER DENYING LEAVE TO APPEAL, AND FOR RECONSIDERATION OF SAID APPLICATION.

Now come 620 Church Street Building Corporation, a corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby and B. K. Goodman, petitioners, by Isaac M. Mills, Theodore E. Rein and Morton C. Chesler, their attorneys, and Emil Rosenthal, petitioner, by Irving L. Block, his attorney, and respectfully move this Honorable Court to vacate the order entered herein denying these petitioners leave to appeal from that certain order of confirmation of a plan of reorganization under Section 77B of the National Bankruptcy Act, entered by the District Court below on March 31, 1936, and respectfully move the court to reconsider said application. In support of the foregoing motion, petitioners present herewith their suggestions.

620 CHURCH STREET BUILDING CORPORATION, IRENE GOODMAN, G. WALTER, M. LONG, A. W. KIBBY and B. K. GOODMAN,
By ISAAC M. MILLS,
THEODORE E. REIN,
MORTON C. CHESLER,
Their attorneys.

EMIL ROSENTHAL,
By IRVING L. BLOCK,
His attorney.

Endorsed: Filed June 9, 1936. Frederick G. Campbell, Clerk.

And afterwards, to wit: On the twenty-sixth day of June, 1936, the following further proceedings were had and entered of record, to wit:

Friday, June 26, 1936.

Court met pursuant to adjournment.

Before:

Hon. Evan A. Evans, Circuit Judge.

Hon. William M. Sparks, Circuit Judge.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

620 Church Street Building Corporation, *et al.*,
Petitioners.

Petition for leave to appeal from an Order of the District Court of the United States for the Northern District of Illinois, Eastern Division.

It is now here ordered by the Court that the motion to vacate the order of this Court denying petition for leave to appeal heretofore entered on May 11, 1936, and for reconsideration of the petition for leave to appeal be, and the same is hereby overruled.

And afterwards, to wit: On the seventeenth day of July, 1936, there was filed in the office of the Clerk of this Court a Notice and Motion for Leave to File a Record, which said Notice and Motion are in the words and figures following, to wit:

No. 5869.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

NOTICE.

To: Defrees, Buckingham, Jones & Hoffman, 38 S. Dearborn St.

George W. Swain, 134 S. LaSalle St.

Gotthard A. Dahlberg, 11 S. LaSalle St.

Pam & Hurd, 231 S. LaSalle St.

Wilhartz, Hirsch & Schanfarber, 38 S. Dearborn St.

Sonnenschein, Berkson, Lautmann, Levinson & Morse, 77 W. Washington St., Chicago, Illinois.

You Are Hereby Notified that on Friday, the 17th day of July, 1936, we shall file with the Clerk of the United States Circuit Court of Appeals for the Seventh Circuit the motion of 620 Church Street Building Corportion, Irene K. Goodman, G. Walter, M. Long, A. W. Kibby, B. K. Goodman and Emil Rosenthal for leave to file a praecipe record in accordance with the Notice and Praecipe heretofore served upon you, a copy of which motion is herewith served upon you. We shall request the Clerk to present said Motion to the Court or any member thereof who may be sitting in the courtroom usually occupied by the Judges of the United States Circuit Court of Appeals for the Seventh Circuit or in cham-

bers on Saturday, July 18th, A. D. 1936. At which time and place you may appear if you so desire.

ISAAC M. MILLS,
THEODORE E. REIN,
MORTON C. CHESLER,
IRVING L. BLOCK,
Chicago, Illinois,
Counsel for Petitioners.

Received a copy of the above and foregoing notice and copy of the Motion therein mentioned this 17th day of July, A. D. 1936.

SONNENSCHEIN, BERKSON, LAUTMANN, LEVINSON & MORSE,
GOTTHARD A. DAHLBERG,
WILHARTZ, HIRSCH & SCHANFARBER,
DEFREES, BUCKINGHAM, JONES & HOFFMAN,
SCOTT MACLEISH & FALK,
PAM & HURD

Endorsed: Filed July 17, 1936. Frederick G. Campbell, Clerk.

No. 5869.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS.

For the Seventh Circuit.

In the Matter of
620 Church Street Building Corporation, a corporation,
Debtor.

MOTION.

Now come petitioners 620 Church Street Building Corporation, Irene K. Goodman, G. Walter, M. Long, A. W. Kibby, and B. K. Goodman by Isaac M. Mills, Theodore E. Rein and Morton C. Chesler, their attorneys and petitioner Emil Rosenthal by Irving L. Block, his attorney, and respectfully

move this Honorable Court for leave to file a praecipe record of the proceedings had in the District Court below, and concerning the order of confirmation leave to appeal from which has been denied by this court; all without prejudice to the several orders and pleadings heretofore filed herein.

620 CHURCH STREET BUILDING CORPORATION, IRENE K. GOODMAN, G. WALTER, M. LONG, A. W. KIBBY and B. K. GOODMAN,

By: ISAAC M. MILLS,
THEODORE E. REIN,
MORTON C. CHESLER,
Their Attorneys,

EMIL ROSENTHAL,

By: IRVING L. BLOCK,
His Attorney.

Endorsed: Filed July 17, 1936. Frederick G. Campbell, Clerk.

And afterwards, to wit: On the twenty-seventh day of July, 1936, there was filed in the office of the Clerk of this Court a Praecipe for Record, which said Praecipe for Record is in the words and figures following, to wit:—

No. 5869.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS.

For the Seventh Circuit.

In the matter of
620 Church Street Building Corporation, a corporation,
Debtor.

PRAECIPE FOR RECORD.

To Frederick G. Campbell, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit:

You will please prepare an authenticated transcript of the record of the proceedings had in the above entitled matter for

transmission to the Supreme Court of the United States in support of a petition for certiorari to be filed by the petitioners herein, and you will please include in such record the following:

1. Notice and Proof of Service of Petition for leave to appeal, filed April 25th, 1936.
2. Petition of 620 Church Street Building Corporation, *et al.* for leave to appeal, filed April 25th, 1936.
3. Joint Assignment of Errors filed by 620 Church Street Building Corporation, *et al.* on April 25th, 1936.
4. Order denying leave to appeal entered May 11, 1936.
5. Memorandum of Court filed May 11, 1936.
6. Notice and Proof of Service filed June 9th, 1936.
7. Motion to vacate order denying leave to appeal, filed June 9, 1936.
8. Order denying motion to vacate entered June 26, 1936.
9. Notice and Motion filed July 17, 1936.
10. This Praecipe for Record.

Respectfully,

I. M. MILLS,
THEODORE E. REIN,
MORTON C. CHESLER,
IRVING L. BLOCK,
Counsel for Petitioners.

July 27, 1936.

We hereby acknowledge receipt of a copy of the foregoing Praecipe for Record.

DON KENNETH JONES,
Counsel for Protective Committee, Respondents.

Endorsed: Filed July 27, 1936. Frederick G. Campbell, Clerk.

UNITED STATES CIRCUIT COURT OF APPEALS.

For the Seventh Circuit.

I, Frederick G. Campbell, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, do hereby certify that the foregoing printed pages, numbered from 1 to 28, inclusive, contain a true copy of the proceedings had and papers filed, made in accordance with the Praecipe for Record filed on July 27, 1936,

In The Matter of 620 Church Street Building Corporation, a corporation,

Debtor,

620 Church Street Building Corporation, *et al.*,

Petitioners.

No. 5869, October Term, 1935, as the same remains upon the files and records of the United States Circuit Court of Appeals for the Seventh Circuit.

In Testimony Whereof I hereunto subscribe my name and affix the seal of said United States Circuit Court of Appeals for the Seventh Circuit, at the City of Chicago, this 29th day of July, A. D. 1936.

FREDERICK G. CAMPBELL,
Clerk of the United States Circuit Court of Appeals for the Seventh Circuit.

(Seal)

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 12, 1936

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Seventh Circuit is granted, and the case is advanced and assigned for hearing immediately following No. 48.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

FILE COPY

Office - Supreme Court
FILED
AUG 8 1936
CHARLES ELMORE CROPLEY
CLERK

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No. 271

In the Matter of

620 CHURCH STREET BUILDING CORPORATION, a corporation, Debtor under Section 77B of the Bankruptcy Act as Amended.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

THEODORE E. REIN,
Counsel for Petitioners.

CHICAGO LAW PRINTING CO., 111 N. WACKER DRIVE (COR. WASHINGTON ST.) TEL. FRANKLIN 6521

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The rights of junior lien holders acquired prior to enactment of Section 77-B including the rights to require a public judicial sale, to bid at such sale and to redeem therefrom within fifteen months are, under the law of the State of Illinois, substantive property rights which cannot be destroyed without consent 27

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No.

In the Matter of

620 CHURCH STREET BUILDING CORPORATION, a corporation, Debtor under Section 77B of the Bankruptcy Act as Amended.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

To the Honorable, the Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

Your petitioners, 620 Church Street Building Corporation, a corporation, Irene Goodman, G. Walter, M. Long, A. W. Kibby, Emil Rosenthal and B. K. Goodman, respectfully pray that a Writ of Certiorari issue to review an order entered May 11, 1936, by the United States Circuit Court of Appeals for the Seventh Circuit, denying petitioners' application for leave to appeal from an order

of the United States District Court, for the Northern District of Illinois, Eastern Division (Barnes, D. J.), entered March 31, 1936, confirming a plan of reorganization in proceedings under Section 77B of the Bankruptcy Act as Amended.

The plan of reorganization was so approved by said District Court without the consent and over the objections of the holders of all of the second and third mortgage indebtedness, and of all of the owners of the capital stock of the Debtor, and over the objection of the Debtor, all being petitioners herein, disregarding substantive property rights of certain of your petitioners and eliminating them from all of the benefits of the reorganization.

Summary Statement of the Case.

Respective Interests of Petitioners.

Petitioner, 620 Church Street Building Corporation, is the owner of the property involved in the proceedings. Petitioners, Irene Goodman, G. Walter, M. Long and A. W. Kibby own all the capital stock of the 620 Church Street Building Corporation. Petitioner, Emil Rosenthal, is the owner of the second mortgage on the property, and petitioner, B. K. Goodman, is the owner of the third mortgage on the property.

The Facts.

On July 12, 1934, the 620 Church Street Building Corporation (hereinafter referred to as Debtor) filed its voluntary petition in the District Court of the United States, Northern District of Illinois, Eastern Division, (Case No. 56564) for reorganization under Section 77B of the Bankruptcy Act.

Thereafter, claims were filed, allowed and classified in said proceedings as follows:

CLASS 2.	First mortgage 6% bonds secured by trust deed dated June 30, 1928, principal amount (interest from January 1, 1931 not being included)	$445,500
CLASS 3.	Second mortgage notes secured by trust deed dated July 13, 1928, principal amount (interest from December 13, 1929, not being included)	40,250
CLASS 4.	Third mortgage note secured by trust deed dated June 3, 1931, principal amount (interest from December 3, 1931 not being included)	27,000
CLASS 5.	Common Stock without par value	1,260 shares

Various appraisals of Debtor's property, ranging from $205,000 to $600,000 were submitted to the District Court.

On or about January 30, 1936, a committee representing first mortgage bondholders filed a plan of reorganization of the Debtor, which provides, in brief, that the property of the Debtor be conveyed to a corporation, also under reorganization under Section 77B, which owns a building adjoining the property of the Debtor, and which has distinct and separate stockholders and creditors. The plan provides that such grantee corporation, in consideration of the conveyance of Debtor's property shall issue a part of its first mortgage bonds and stock to be distributed solely among the holders of the first mortgage bonds of the

Debtor. No payment or consideration of any kind to the holders of the second mortgage, to the holders of the third mortgage, or to the stockholders of the Debtor is contemplated. It does not provide for a public sale of Debtor's property, and makes no provision whereby the holders of the second mortgage, third mortgage or stockholders of the Debtor may bid for the property. Furthermore, it does not provide and, in fact, wipes out, the right of redemption of Debtor's property by any of the petitioners.

The plan was accepted by the Committee in behalf of the holders of more than two-thirds of the first mortgage bonds, but no acceptance of the plan was filed by the holders of any of the claims based upon the second mortgage notes, or the third mortgage note, nor by any of the stockholders of the Debtor, all of whom filed objections to said plan.

On the 31st day of March, 1936, the District Court entered an order of confirmation (R. 12) from which leave to appeal was sought in the United States Circuit Court of Appeals for the Seventh Circuit. The order of confirmation finds, among other things, that the property of the Debtor has a fair market value of $245,025, that, therefore, there is no equity in said estate over and above the $445,500 of principal amount of first mortgage bonds, that the Debtor is accordingly insolvent, and that the consent of a majority of the stockholders of the Debtor is not a prerequisite to the confirmation of the plan (R. 14, 15). Said order, in paragraph 12 thereof, purports to appraise all claims filed in Class 3, (the second mortgage notes), and all claims filed in Class 4, (the third mortgage note), to be of no value, and that, therefore, the consents of two-thirds in amount of claims allowed in Classes 3 and 4 were not prerequisite to the confirmation of the plan.

Thereafter, petitioners filed a joint petition for leave to appeal from said order of confirmation, and likewise filed a joint assignment of errors. On May 11th, 1936, the Circuit Court of Appeals denied petitioners leave to appeal.

Questions Presented.

The questions accordingly presented by this application are as follows:

(1) Does Section 77B of the Bankruptcy Act authorize the District Court to approve a plan of reorganization which has not received the consent of two-thirds of each class of claims secured by junior liens, and which does not provide adequate protection for the payment of such claims?

(2) Are the rights of owners of junior liens acquired prior to the enactment of Section 77B of the Bankruptcy Act as Amended, including (a) the right to have the property subject to the junior liens sold at a public sale, and (b) the right to bid at such sale, and (c) the right to make redemption from a sale at the bid price in accordance with the Statutes of the State of Illinois, property rights, within the purview of the Fifth Amendment of the Constitution of the United States, of which the owners may not be divested without their consent?

Reasons Relied Upon for Allowance of the Writ.

The reasons respectfully presented for the allowance of the Writ of Certiorari in the instant case, are as follows:

1. **The conflict between the decision of the District Court which the Circuit Court of Appeals declined to review, and the decision of the Supreme Court of the United States.**

The ruling of the Circuit Court of Appeals is in conflict with the recent decision of this Court involving the same substantive rights. (*Louisville Joint Stock Land Bank* v. *Radford,* 295 U. S. 555)

2. **Conflict in the decision of the Circuit Courts of Appeal.**

The refusal of the Circuit Court of Appeals to grant petitioners leave to appeal and the memorandum filed by the Court (R. 21), conflicts with the decision of the Sixth Circuit (*In Re*: *Tennessee Publishing Co.,* 81 Fed. 2nd 463), and also conflicts with the decision of the Second Circuit (*In re*: *Murel Holding Corporation,* 75 Fed. 2nd 941), and is also in conflict in some respects with its own recent decision (*In re*: *Georgian Hotel Corporation, Debtor,* 82 Fed. 917).

3. **Failure to observe and follow local and Federal law affording protection of property rights.**

Both the law of the State of Illinois and the Federal law recognize that the right of redemption of lien holders is a right in specific property, which cannot be taken away by subsequently enacted legislation in violation of the Fifth Amendment to the Constitution of the United States, (*Louisville Joint Stock Land Bank* v. *Radford,* 295 U. S. 555; *Parker* v. *Dacres,* 130 U. S. 43; *Bronson* v. *Kinzie,* 1 Howard 311; *Fitch* v. *Wetherbee,* 110 Ill. 475, 492; *Buszin* v. *Martinowica,* 178 Ill. App. 519, 523).

4. Importance of the questions involved.

Uncertainty as to the meaning of a law as important in economic affairs as Section 77B should be removed by decision as rapidly as possible, and it is respectfully submitted, when such a case is presented squarely raising significant issues, it is advisable that this court give to the bar and to the public the benefit of its considered judgment.

Considerations of practical justice recommend that the prayer of the petition for Writ of Certiorari be allowed. Numerous cases involving junior liens are pending in the District Court, and their disposition will be facilitated by a decision of this Court. If petitioners be compelled to await final decree in the proceedings below, and then appeal as of right to the Circuit Court of Appeals for the Seventh Circuit, (which Court already by its memorandum filed below (R. 21) indicated that it will decide the merits of the proceeding contrary to petitioners' contentions), much time will elapse during which steps will be taken affecting the title to the property of Debtor, and a substantial sum expended to put the plan of reorganization into effect.

WHEREFORE, your petitioners respectfully pray that a Writ of Certiorari issue out of and under the seal of this Honorable Court to review the decree of the Circuit Court of Appeals for the Seventh Circuit and review the decree of the District Court, and that said decrees of said courts may be reversed.

THEODORE E. REIN,
Counsel for Petitioners.
10 South LaSalle Street,
Chicago, Illinois.

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No.

In the Matter of

620 CHURCH STREET BUILDING CORPORATION, a corporation, Debtor under Section 77B of the Bankruptcy Act as Amended.

BRIEF IN SUPPORT OF PETITION FOR THE WRIT OF CERTIORARI.

STATEMENT.

A.

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240 of the Judicial Code as amended; United States Code, Title 28, Section 347.

B.

The Statute Involved.

The statute involved is Section 77B of the Bankruptcy Act as amended. United States Code, Title 11, Section 207. Petitioners seek a construction of paragraph b of Section 77B, the provisions of which pertinent to this inquiry are as follows:

> "A plan of reorganization within the meaning of this Section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise;
> * * *
>
> (5) Shall provide in respect of each class of creditors of which less than two-thirds in amount shall accept such plan (unless the claims of such class of creditors will not be affected by the plan, or the plan makes provision for the payment of their claims in cash in full), provide adequate protection for the realization by them of the value of their interests, claims, or liens, if the property affected by such interests, claims, or liens is dealt with by the plan, either as provided in the plan
>
> (a) By the transfer or sale of such property subject to such interests, claims, or liens or by the retention of such property by the debtor subject to such interests, claims, or liens, or
>
> (b) By a sale free of such interests, claims, or liens at not less than a fair upset price and the transfer of such interests, claims, or liens to the proceeds of such sale; or

(c) By appraisal and payment either in cash of the value either of such interests, claims, or liens, or, at the objecting creditors' election, of the securities allotted to such interests, claims, or liens under the plan, if any shall be so allotted; or

(d) By such method as will in the opinion of the judge, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection."

C.

Judgment Sought to be Reviewed.

The Circuit Court of Appeals for the Seventh Circuit denied petitioners' application for leave to appeal on May 11, 1936 (R. 22), and on June 26, 1936 denied petitioners' motion for reconsideration of said petition for leave to appeal (R. 24).

The order sought to be reviewed in the Circuit Court of Appeals is an order of confirmation of the District Court of the United States approving and confirming a plan of reorganization under Section 77-B of the Bankruptcy Act, entered by said District Court March 31, 1936.

In connection with the order denying leave to appeal the Circuit Court of Appeals filed a memorandum (R. 21) in which said court stated that the District Court did not err in ruling that if the property involved were not worth the amount of the first mortgage indebtedness, the junior interests had no equity to be protected, thus treating the interests of petitioners as possessing a temporary, monetary value alone, based upon opinion evidence, and disregarding petitioners' substantive rights to require a public sale, to be permitted to bid thereat and to redeem from such sale.

D.

Statement of the Nature of the Case.

A petition for the reorganization of the debtor corporation was filed pursuant to Section 77-B of the Bankruptcy Act, as amended, the property of the debtor consisting of a store and office building located in the City of Evanston, in the State of Illinois. The plan of reorganization as confirmed requires the debtor to convey its property to the corporation owning the adjoining premises, the grantee corporation being a distinct legal entity with its own stockholders and creditors. In consideration for the conveyance the grantee is to issue its bonds and some common stock, all of which will go to the holders of the first mortgage bonds of the debtor. The debtor, the debtor's stockholders and the holders of all of its second and third mortgage indebtedness will receive nothing. The District Court, upon opinion evidence, found that the value of the debtor's property was less than the amount of the first mortgage encumbrance and that, therefore, the claims of the holders of the second and third mortgage indebtedness were of no value, there being no equity for them in the property, and that, accordingly, nothing of value should be distributed to them. The order provided, further, that the consent of the petitioners here who hold all of the second and third mortgage indebtedness was not prerequisite to the confirmation of the plan (R. 15). The court found that the plan provides adequate protection for the realization by the holders of the second and third mortgage indebtedness under the circumstances of the case, such claims being of no value (R. 15).

Petitioners contended that their rights did not depend upon their immediate or temporary ability to collect in

terms of money and that the plan disregarded and violated the right to require a judicial sale, to bid at such sale and to redeem in the event that the property was struck off to some other bidder. These rights the District Court disregarded and, thereupon, petitioners prayed for leave to appeal to the United States Circuit Court of Appeals for the Seventh Circuit where petitioners contended that a review of the order of the District Court was necessary to determine the question as to whether or not Section 77-B of the Bankruptcy Act authorizes plans of reorganization under the circumstances of the case. The Circuit Court of Appeals declined to review and, therefore, petitioners present this application for the writ of certiorari.

To avoid needless repetition the court is respectfully referred to the fuller statement of the case contained in the petition for the Writ of Certiorari with which this brief is filed (*ante* page 2).

E.

Specification of Errors.

1. The courts below erred in holding that the approval of a plan of reorganization by the District Court may be ordered without the consent of two-thirds of the holders of recognized classes of claims secured by junior encumbrances, without compensation to them and without making provision for their protection.

2. The courts below further erred in refusing to hold that the rights of junior lien holders, acquired prior to the enactment of Section 77-B, including the right to insist upon a public sale, the right to bid thereat and the right to redeem within fifteen months after a sale to a successful bidder are, under the law of Illinois, property rights which cannot be disregarded or destroyed without consent.

SUMMARY OF THE ARGUMENT.

I.

The approval of the plan of reorganization by the District Court without the consent of the holders of two-thirds in amount of secured junior indebtednesses, without compensation to them and without making provision for their protection, violates the provisions of Section 77-B of the Bankruptcy Act, as amended.

A

Section 77-B requires the consent of two-thirds of any recognized class of creditors to a proposed plan of reorganization unless their claims are not affected or unless the plan makes provision for payment to them in full or unless the plan makes other adequate protection for the realization of the value of their interests, if such interests be affected. The methods for assuring such adequate protection are described in the Act itself, none of which methods was adopted by the plan.

Section 77-B of the Bankruptcy Act as amended, United States Code, Title 11, Section 207, paragraph b.

B

That the rights of classes of creditors must be so protected in the absence of the required consent, is recognized by the decided cases.

In re Hotel Charles Co., 12 Fed. Supp. 734, 736 (D. C. Mass.);

In Re Murel Holding Corp., 75 Fed. (2nd) 941, 942 (C. C. A. 2nd);

Francisco Building Corporation, Ltd. v. *Battson*, 83 Fed. (2nd) 93, (C. C. A. 9th);

Tennessee Publishing Co. v. *American National Bank*, 81 Fed. (2nd) 463, 468, (C. C. A. 6th);

Louisville Joint Stock Land Bank v. *Radford*, 295 U. S. 555, 589, 590.

C

The true value of property in a reorganization proceeding is not a foreclosure, or forced sale value, reorganization contemplating not a present liquidation but a continuance of life into the future.

Warner Brothers Pictures v. *Lawton-Byrnes-Bruner Ins. Agency*, 79 Fed. (2nd) 804, 817, (C. C. A. 8th).

D

The present or immediate collectibility of a claim is not the true or full measure of a claimant's rights and interests.

E

If the value of the property be as low as the amount found by the court then, it may be immediately seen, a public judicial sale would permit petitioners to bid within the same low range of prices and would afford them an opportunity to redeem, within fifteen months, by payment of the amount successfully offered at the sale. It is thus apparent that the value of petitioners' interests cannot be determined by a present appraisal of the debtor's property upon the theory of a liquidation price at a forced sale.

II.

The rights of junior lien holders acquired prior to the enactment of Section 77-B, including the right to insist upon a public, judicial sale, the right to bid at such sale, and the right to redeem within fifteen months after a sale to a successful bidder are, under the law of the State of Illinois, property rights which cannot be disregarded or destroyed without consent.

A

This court has held that no Bankruptcy Act may undertake to destroy the substantive and previously acquired rights of creditors.

Louisville Joint Stock Land Bank v. *Radford*, 295 U. S. 555, 589.

B

This court has also held that in order to determine what are substantive property rights, recourse must be had to the law of the State where the litigation is pending.

Louisville Joint Stock Land Bank v. *Radford*, 295 U. S. 555, 590.

C

Under the Law of Illinois, the mortgagor possesses the right to redeem for the period of twelve months, and a judgment creditor for the period of fifteen months, after sale.

Cahill's Illinois Revised Statutes, 1931, Ch. 77, paragraphs 18 and 20.

D

This court has held that the right of redemption as conferred by a state statute is a rule of property and is a substantive property right.

Brine v. *The Hartford Fire Insurance Co.*, 96 U. S. 627, 634, 636;
Parker v. *Dacres*, 130 U. S. 43, 48;
Bronson v. *Kinzie*, 1 How. 311, 315.

E

The courts of Illinois recognize the absolute nature of the right of redemption.

Fitch v. *Wetherbee*, 110 Ill. 475, 492;
Buszin v. *Martinowicz*, 178 Ill. App. 519, 523;
In Re Georgian Hotel Corporation, 82 Fed. (2nd) 917, 920.

F

Because the right of redemption is a substantive right constituting a rule of property in Illinois, the attempted destruction of that right in the approval of the plan of reorganization is clearly erroneous.

ARGUMENT.

I.

The approval of the plan of reorganization by the District Court without the consent of the holders of two-thirds in amount of secured junior indebtednesses, without compensation to them and without making provision for their protection, violates the provisions of Section 77B of the Bankruptcy Act, as amended.

For the purposes of this application, under the theory that the greater must include the smaller, only the rights of petitioners who hold all of the evidences of the second and third mortgage indebtednesses of the debtor, will be treated.

There can be no question that those of the petitioners who hold all of the second and third mortgage indebtedness and whose claims were classified and allowed as valid, are invested with all of the rights inherent in their respective contracts,—rights which are specifically recognized by the laws of the State of Illinois. The District Court, however, finding that the temporary value of the Debtor's property, from a present sale standpoint, did not equal the amount of the first mortgage indebtedness, proceeded to eliminate these secured creditors from consideration and, without their consent and over their objection, approved the plan which provides for the conveyance of the Debtor's property to the corporation which owns the adjoining structure, in consideration of the delivery of bonds and stock to be issued by the grantee corporation

to the holders of the first mortgage indebtedness of the Debtor. While the building of the Debtor and that of the grantee corporation adjoin and possess certain physical, cooperative facilities, such as a common entrance, a connecting bridge, elevator service in the adjoining building, and a heating system therein which furnishes heat to the Debtor's tenants,—the building of the Debtor is so constructed that these cooperative features are not permanently essential and, at comparatively small cost, the Debtor's building could be made self-sufficient.

Notwithstanding that the two corporations are separate legal entities, each with its own stockholders and creditors, they were treated together in such fashion that, as the result of correlated plans of reorganization, the corporation owning the adjoining piece obtains the conveyance of the Debtor's property in consideration of the delivery of $222,750.00 par value of the first mortgage bonds of the grantee corporation, out of a total issue of $668,250.00, and twenty-five per cent. of the capital stock of the grantee, all of which bonds and stock go to the holders of the first mortgage indebtedness of the Debtor.

No provision is made for the protection of the second and third mortgage creditors and no payment to them contemplated, the court contenting itself with the finding that by reason of a present, hypothetical value of the Debtor's property, resting upon opinion alone, they possessed no equity in the property and their security was, accordingly, worthless. As will be seen in the succeeding point, by their contracts which existed long before Section 77B was contemplated, these petitioners had the right to require a judicial sale. This was denied by the plan. They had the right to bid at such sale. This opportunity was likewise eliminated. Above all, they had the continuing and substantive right to redeem from judicial sale,

under the pre-existing law of the State of Illinois for fifteen months after any such sale should take place. This right was forever cut off by the approved plan.

It may be observed, in passing, that the wide difference in views of the experts as to fair cash "market" value, when there is no market to furnish a standard of comparison, indicates, if anything, the inevitably inconclusive and unsatisfactory nature of partisan opinions.

What the District Court neglected to observe was that if the Debtor's property actually had the low value ascribed to it by the "depression experts", the price paid by a successful bidder at foreclosure or at any other liquidation sale would be the same low price at which petitioners could redeem had their right so to do been recognized.

How petitioners were treated appears from the order confirming the plan. The District Court found "that there is no equity over and above the $445,500.00 principal amount of Carlson Annex Bonds outstanding * * *; that the Debtor is accordingly insolvent; that the stockholders are not entitled to participate in the plan and that their acceptance * * * is not a prerequisite to the confirmation of the plan" (R. 14, 15).

The court further found that, based upon the evidence and testimony concerning the value of the property, the court appraised the claims allowed in Classes 3 and 4 (petitioners' claims as second and third mortgage creditors), to be of no value, there being no equity in the property and "accordingly no securities, cash or any other thing of value shall be distributed under the plan in respect of any of the claims allowed in Classes 3 and 4, and the acceptance of the plan by the holders of such claims is not a prerequisite to the confirmation of the Plan (R. 14, 15).

The court then made the following surprising finding:

> "The court further finds that the foregoing method of treatment of the holders of claims in Classes 3 and 4 provides adequate protection for realization of the holders thereof of the value thereof under and consistent with the circumstances of the case, the same being of no value" (R. 15).

The erroneous assumption by the District Court that the alleged, temporary, sale value of property is the sole measure of property rights, disregarding the substantive, continuing right to redeem and the other rights of the petitioners, may thus be plainly seen.

Therefore, on this branch of the controversy, the question is can the holders of junior mortgage indebtednesses, recognized as valid claimants in specified classes, be wholly disregarded and their rights eliminated from beneficial participation in a plan of reorganization without their consent, without compensation, and without any provision for their protection?

This question is answered by the Act itself.

That Section 77B of the Bankruptcy Act requires the consent of two-thirds in amount of each class of creditors, or in the absence thereof, compensation or adequate protection for each of such classes, plainly appears from the language of the statute itself. Subdivision (b) of Clause 5 is as follows:

> "A plan of reorganization within the meaning of this Section shall include provisions for modifying or altering the rights of creditors generally, or any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; * * * shall provide in respect of each class of creditors of which less than two-thirds in amount shall ac-

cept such plan (unless the claims of such class of creditors will not be affected by the plan, or the plan makes provision for the payment of their claims in cash in full), provide adequate protection for the realization by them of the value of their interests, claims, or liens, if the property affected by such interests, claims, or liens, is dealt with by the plan, as provided in the plan

(a) By the transfer or sale of such property subject to such interests, claims, or liens, or by the retention of such property by the debtor subject to such interests, claims, or liens, or

(b) By a sale free of such interests, claims, or liens at not less than a fair upset price and the transfer of such interests, claims, or liens to the proceeds of such sale; or

(c) By appraisal and payment either in cash of the value either of such interests, claims, or liens, or, at the objecting creditors' election, of the securities allotted to such interests, claims, or liens under the plan, if any shall be so allotted; or

(d) By such method as will in the opinion of the judge, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection."

Dissecting this provision, we find:

That a plan of reorganization may be adopted and approved which may modify or alter rights of creditors generally or any class of them, provided, however,

(1) That two-thirds of each class of creditors accept such plan.

(2) That such acceptance is unnecessary where the creditors of a given class are not affected.

(3) That such acceptance is unnecessary when the plan makes provision for the payment of their claims in cash in full, and

(4) That such acceptance is unnecessary if the plan provide adequate protection for the realization of the value of the interests, claims or liens dealt with by the plan.

Since petitioners who are the holders of all of the secured claims in classes 3 and 4 are entirely wiped out, it cannot be said that their interests are not affected. If, then, classes of claims be affected, and if payment in cash is not provided for, then, in the absence of consent, the ensuing language of the law becomes applicable which makes specific the requirement that *adequate protection* be accorded for the realization of such claims and interests and describing the means and methods of affording such protection.

None of these methods was adopted for the protection of the interests of those of the petitioners here who hold junior securities. There was no transfer or sale subject to their interests. There was no retention by the debtor of the property, subject to their interests. There was no sale at a fair, upset price and a transfer of the claims to the proceeds of the sale. There was no appraisal of the interests and claims of these petitioners and, obviously, this could not have been done as it would have involved placing a value on the rights of the petitioners to bid at the sale of the property and to redeem at the sale price for a period of fifteen months after the sale in the event that the property had been bid in by others. The only appraisal that was made by the court involved the valuation of the debtor's property as a whole, and in so doing the court gave to it "a foreclosure price".

In passing, it may be observed that reorganization under Section 77B, or by any other means, contemplates continued existence, continued operation, continued interests, even if altered or modified. A sale of all of the assets of a business, lock, stock and barrel, is not reorganization but liquidation in the strictest sense. It was upon the *liquidation theory* that the District Court valued the property of the debtor.

As was said in *Warner Brothers Pictures* v. *Lawton-Byrns-Bruner Ins. Agency Co.*, 79 Fed. (2nd) 804, 817 (C. C. A. 8th):

> "However, the foreclosure sales prices are by no means measures of the values of the properties for corporation purposes. Prices at foreclosure sales are notoriously under actual values (unless the property sold has a free open market value, as listed securities, grain, live stock, etc.). Such dispositions are forced sales. It is this forced sale value which is in mind when adequacy of bids at foreclosure is considered. It is the actual fair value at a free sale that is in mind when considering the value of property used for payment of corporate stock and bonds issued."

So, in the case at bar, the actual fair value at a free sale should have been the subject matter of the court's consideration since the property of the debtor was conveyed to the grantee and payment made in bonds of the grantee corporation. Under the announced decisions of the United States Courts inferior to the Supreme Court, it would seem that the judges are of the prevailing opinion that Section 77-B requires adequate protection or compensation or, in their absence, consent.

In the matter of *Hotel Charles Co.,* 12 Fed. Supp. 734, 736, (D. C. Mass.) Judge Brewster said:

> "If any creditor claims a lien upon the property affected by the plan of reorganization and he does not belong to a class of duly assenting creditors, the plan cannot be confirmed unless it provides *adequate protection* for the realization by the creditor of the value of his interest or lien in or upon the property."

The Circuit Court of Appeals of the Second Circuit in *In Re Murel Holding Corporation,* 75 Fed. (2nd) 941, speaking through Judge Hand who rendered the opinion said at page 942:

> "Normally it was expected that consents should be obtained. If they were not, the plan must 'provide adequate protection for the realization by them' the dissenting class, 'of the full value of their interest, claims or liens.' This may be done in four ways: (a) The liens may be merely kept in *statu quo.* (b) The property may be sold free and clear and the liens attached to the proceeds. (c) The value of the liens may be appraised and paid, or, if the objectors prefer, the same course might be taken with any new securities. (d) The last is not, properly speaking a 'method' at all; it merely gives power generally to the judge 'equitably and fairly' to 'provide such protection' * * * It is plain 'adequate protection' must be *completely compensatory.*"

Going to the other end of the continent, the Circuit Court of Appeals of the Ninth Circuit in *Francisco Building Corporation, Ltd. v. Battson,* 83 Fed. (2nd) 93 (C. C. A. 9th) completely approved the preceding opinion by Judge

Hand in a case where it was contended that it was unnecessary to secure the consent of bondholders and creditors because the proposed plan "came under Section 77-B of the Bankruptcy Act".

If the statute be construed as authorizing the erasure of rights of second and third mortgage bondholders, without their consent and without compensation or protection, then, in principle, rights of first mortgage bondholders may be similarly, and without their consent, adversely affected. While the rights of holders of junior securities are subject, in material respects, to the rights of creditors who are senior to them, such junior holders, nevertheless, do possess rights which are in no manner subject to, or eliminated by, the presence of an antecedent first mortgage. The first mortgagee cannot successfully object to the request of junior mortgage bondholders to have a public sale, nor can such first mortgagee deny the rights of creditors inferior to him to bid at such sale. Certainly the important property right to redeem becomes solidified when the foreclosure by the first mortgagee reaches the final result of a sale. To deny to whole classes of creditors rights which are not in any manner affected by the presence of a senior mortgage, and to hold that Section 77-B permits such denial, is to give to the Statute an unconstitutional interpretation refuted by the language of the Act itself.

In *Tennessee Publishing Co.* v. *American National Bank*, 81 Fed. (2nd) 463, (C. C. A. 6th) the Court said at page 468:

> "We are here concerned only with the validity of a clause which provides for adjustment of debts without the consent of creditors. It has long been settled that provisions in bankruptcy statutes authorizing compositions have never been held to invalidate

them. This is because a composition is a matter of agreement between the bankrupt and his creditors as a class, with the will of the majority imposed upon the minority. *In re Lane* (D. C.) 125 F. 772, 773; *Cumberland Glass Mfg. Co.* v. *DeWitt*, 237 U. S. 447, 452, 35 S. Ct. 636, 59 L. Ed. 1042.

"We confine ourselves to the provisions of subsection (b) (5), which outline a method for adjustment of claims of non-assenting creditors, and inquire as to their validity in the light of the due process clause. Upon this issue we view the decision of the Supreme Court in *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, 55 S. Ct. 854, 79 L. Ed. 1593, 97 A. L. R. 1106, controlling. Here, under Tennessee law, as there under Kentucky law, the lien holders had the right under their contract to retain the lien until the indebtedness secured was paid, the right to realize upon the security by a judicial public sale, the right to determine when such sale should be held, subject only to the discretion of the court, the right to protect their interest in the property by bidding at such sale, the right to have the mortgaged property devoted primarily to the satisfaction of the debt; and the right to control the property meanwhile during the period of default, subject only to the discretion of the court, and to have the rents and profits during such period applied to the satisfaction of the debt. These rights are substantive property rights, and any invasion of them under the authority of the present statute is as clearly violative of the due process clause of the Fifth Amendment as it was in the *Radford* Case."

By all processes of logical reasoning, this court, in *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S.

555 rendered an opinion, the inevitable result of which is to confirm petitioners' contentions. There this court held the Frazier-Lemke Act unconstitutional because it proposed to deny property rights under a mortgage existing prior to the enactment of the statute. As the court said at page 589:

> "Because the act is retroactive in terms and as here applied purports to take away rights of the mortgagee in specific property, another provision of the Constitution is controlling.
>
> "The Bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment."

At page 589 of the opinion the Court said:

> "But the effect of the act here complained of * * * is the taking of substantive rights in specific property acquired * * * prior to the act."

Unless it is possible to say, therefore, that the rights of junior security holders are dependent wholly upon a temporary value based upon opinion and found by the court and unless the substantive, although not monetary, rights to require a public sale, to be permitted to bid thereat, and to redeem, are regarded as of no legal significance, it must follow with mathematical inevitability that any attempt to disregard and destroy such rights is an invalid exercise of governmental power. If a statute makes such attempt it is unconstitutional, and if a court by its order produces the same result under a statute which does not authorize it, its order is invalid. In the one case it is a legislative, and in the other a judicial, invasion of private rights.

Whether or not the right to redeem, for example, be a substantive right and, as such, indestructible under the provisions of any subsequently enacted legislation depends upon the law of the State of Illinois. As was said by Mr. Justice Brandeis in the *Radford* case at page 590:

> "In order to determine whether rights of that nature have been taken, we must ascertain what the mortgagee's rights were before the passage of the act. We turn, therefore, first to the law of the state."

This brings the present discussion to the consideration of the nature and inviolability of the rights of petitioners which are in no manner subject to the rights of creditors senior to them.

II.

The rights of junior lien holders, acquired prior to the enactment of Section 77-B, including the right to insist upon a public sale, the right to bid at such sale, and the right to redeem within fifteen months after a sale to a successful bidder are, under the law of the State of Illinois, property rights which cannot be disregarded or destroyed without consent.

That the rights of junior lienholders to require a public sale, to be permitted to bid thereat and to redeem from such sale, are substantive property rights, is not open to question under the decisions of this court and of the Supreme Court of the State of Illinois.

Mr. Justice Brandeis in the *Radford* case said at page 583:

> "No bankruptcy act had undertaken to modify in the interest of either the debtor or other creditors any substantive right of the holder of a mortgage valid under federal law."

In the same case, speaking of bankruptcy acts which had expressly or impliedly authorized the marshalling of liens on property of the bankrupt and the sale of such property free of encumbrances but directing that the rights of lien holders be transferred to the proceeds of such sale, the Court said at page 584:

> "But there had been no suggestion that such a sale could be made to the prejudice of the lienor, in the interest of either the debtor or of other creditors. By the settled practice, a sale free of liens will not be ordered by the bankruptcy court if it appears that the amount of the encumbrance exceeds the value of the property. And the sale is always made so as to obtain for the property the highest possible price. No court appears ever to have authorized a sale at a price less than that which the lien creditor offered to pay for the property in cash. Thus, a sale free of liens in no way impairs any substantive right of the mortgagor; and such a sale is not analogous to the sale of the bankrupt provided for by Paragraph 7 of the Frazier-Lemke Act."

Commenting upon compositions in bankruptcy, Mr. Justice Brandeis said at page 585:

> "So far as concerns the debtor, the composition is an agreement with the creditors in lieu of a distribution of the property in bankruptcy—an agreement which 'originates in a voluntary offer by the bankrupt, and results, in the main, from voluntary acceptance by his creditors.' * * * In no case of composition is a secured claim affected except when the holder is a member of a class; and then only when the composition is desired by the requisite majority and is approved by the court. Never, so far as appears, has any com-

position affected a secured claim held by a single creditor. Compositions are comparable to the voluntary adjustment with the mortgagee provided for in Paragraph 3 of the Frazier-Lemke amendment. They are not analogous to the so-called adjustment *compelled* by paragraph 7."

Under the law of Illinois, the right to redeem is clearly set forth in its statute which provides that a mortgagor shall have the right of redemption for a period of twelve months after sale, and that judgment creditors possess a similar right for fifteen months thereafter.

The Illinois Statute upon redemption, Cahill's Illinois Revised Statutes, 1931, ch. 77, paragraph 18, provides:

> "Any defendant, his heirs, administrators, assigns, or any person interested in the premises, through or under the defendant, may, within twelve months from said sale, redeem the real estate so sold by paying to the purchaser thereof, his executors, administrators or assigns or to the sheriff or master in chancery, or other officer who sold the same, or his successor in office, for the benefit of such purchaser, his executors, administrators, or assigns, *the sum of money for which the premises were sold or bid off*, with interest thereon at the rate of six per centum per annum from the time of such sale, whereupon such sale and certificate shall be null and void."

Paragraph 20 of this Statute deals with redemption by creditors and provides:

> "If such redemption is not made, any decree or judgment creditor, his executors, administrators or assigns may, after the expiration of twelve months and within fifteen months after the sale, redeem the prem-

ises in the following manner: Such creditor, his executors, administrators or assigns may sue out an execution upon his judgment or decree, and place the same in the hands of the sheriff or other proper officer to execute the same, who shall indorse upon the back thereof a levy of the premises desired to be redeemed; and the person desiring to make such redemption shall pay to such officer the amount for which the premises to be redeemed were sold, with interest thereon at the rate of six per centum per annum from the date of the sale, for the use of the purchaser of such premises, his executors, administrators or assigns, whereupon such officer shall make and file in the office of the recorder of the county in which the premises are situated a certificate of such redemption, and shall advertise and offer the premises for sale under said execution as in other cases of sale or execution."

In *Brine* v. *The Hartford Fire Insurance Company*, 96 U. S. 627, this court held that the statute of Illinois which so allowed redemption confers a substantial right and thereby becomes a rule of property. The court said at page 636:

"The Legislature of Illinois has prescribed, as an essential element of the transfer by the courts in foreclosure suits, that there shall remain to the mortgagor the right of redemption for twelve months, and to judgment creditors a similar right for fifteen months, after the sale, before the right of the purchaser to the title becomes vested. This right, as a condition on which the title passes, is as obligatory on the Federal Courts as on the State Courts, because in both cases it is made a rule of property by the Legislature, which had the power to prescribe such a rule. • • • But there is another view of the question which

is equally forcible, and which leads to the same result. All contracts between private parties are made with reference to the law of the place where they are made or are to be performed. Their construction, validity and effect are governed by the place where they are made and are to be performed, if that be the same as it is in this case. It is, therefore, said that these laws enter into and become a part of the contract."

Again, in *Parker* v. *Dacres*, 130 U. S. 43, Mr. Justice Harlan, delivering an opinion of this court, said at page 48:

> "In many of the states the right to redeem within a prescribed time after sale under a decree of foreclosure is given, in certain cases, by statute. This right, when thus given, is a substantial one, to be recognized even in the Courts of the United States sitting in equity, because the statute constitutes a rule of property in the State that enacts it. *Brine* v. *Hartford F. Ins. Co.*, 96 U. S. 627 (ad: 858); *Hammock* v. *Farmers Loan & T. Co.*, 105 U. S. 77; 88 (26; 1111, 1115); *Mason* v. *Northwestern Mut. L. Ins. Co.*, 106 U. S. 164 (27: 130); *Conn. Mut. L. Ins. Co.* v. *Cushman*, 108 U. S. 51, 63 (27: 648, 652)."

The Supreme Court of Illinois has repeatedly confirmed the statute of redemption of its own state. Thus in *Fitch* v. *Wetherbee*, 110 Ill. 475, the court, in commenting upon the absoluteness of the right of redemption, said at page 492:

> "The right of redemption given by the statute to a decree or judgment creditor is not affected by a failure of the court to provide in its decree for the sale of real estate, with the privilege of redemption. It is the statute that gives the right of redemption, and not the decree of the court. In a case where the stat-

ute authorizes a redemption from a sale, a clause in the decree ordering the sale that declares the sale shall be absolute, will not bar that right. That portion of the decree will be regarded as inoperative, and a redemption will be allowed as in other cases. Nor does it make any difference whether the sale was conducted by an officer of the law or by one appointed by the court to perform that special duty."

Other illuminating cases upon the subject are:

Bronson v. *Kinzie,* 1 How. 311, 315.
Buszin v. *Martinowicz,* 178 Ill. App. 519, 523.
Turk v. *Mayberry,* 121 Pac. 665, 669 (Okla. 1912).

The right to redeem by paying the price bid at the foreclosure sale, continuing as it does for 15 months, gives to junior security holders a valuable option. Frequently the first mortgagee is the successful bidder, and, as frequently, he bids less than the amount of the indebtedness, as is evidenced by the well nigh invariable practice of taking deficiency decrees. Particularly valuable is the right of redemption in a rising market. Whether valuable or not from a monetary standpoint, however, it is absolute and vested and it is not for the court to put a price upon it or to declare it valueless. As was said in *Cram* v. *Cottrell,* 48 Neb. 646:

"The plaintiffs had a legal right to redeem, whether or not the exercise of that right would be profitable to them. It was for them to determine whether they should exercise the right, and not for the court to deny them the right because, in its opinion, its exercise would not be profitable."

The Circuit Court of Appeals for the Seventh Circuit, *In re Georgian Hotel Corporation,* 82 Fed. (2nd) 917, rec-

ognized that the right of subordinate creditors to redeem should be observed by the court saying in page 920:

> "While it is not likely that at the present time the subordinate creditors would have realized anything if the first mortgage had been foreclosed, these creditors would, for three months after one year following the foreclosure sale, have had a right of redemption—a right which might have been valuable. And there is the possibility that, with a substantial 'comeback' in affairs, property values may increase sufficiently to give the debtor a substantial equity in the property of which these creditors would have the benefit."

Because the right of redemption is a substantive right and constitutes a rule of property in the State of Illinois, and since this right was disregarded by the order which approved the plan of reorganization, it necessarily follows that the order of the District Court was invalid. Carrying with it, as it did, the announcement of a practice and of a construction placed upon Section 77B by the United States Courts administering such proceedings, the Circuit Court of Appeals should have permitted a complete presentation of the question by a full review of the action of the lower court.

CONCLUSION.

The debtor corporation in the instant case has not been reorganized by the plan approved by the District Court. It has, on the contrary, been sold out and wound up by compelling it to convey all of its property to another, separate, legal entity. This constitutes strict liquidation and foreclosure in the most rigorous sense. The legislative thought which induced the passage of Section 77B was not destruction and termination, but protection and continuation. It seems to contemplate settlement and reorganization by the interested parties themselves under the watchful supervision of the court. No matter what may have been the legislative philosophy which induced its passage, however, a careful examination of the provisions of the Act demonstrates that no whole class of lien claimants can be summarily eliminated under its terms. No state law, no federal law, no decision by a court which attempts to destroy acknowledged, vested and substantive property rights has ever been approved by this court, and yet, as has been seen, this is exactly the result accomplished by the decree of the District Court in confirming the plan of reorganization.

A review of the case at bar will decide whether or not such a result is possible under Section 77B and will establish a timely and needed precedent.

Respectfully submitted,

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OCT 29 1936
CHARLES ELMORE CROPL
CLERK

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No. 271

IN THE MATTER OF THE
620 CHURCH STREET BUILDING CORPORATION,
A CORPORATION, DEBTOR UNDER SECTION 77B OF THE BANKRUPTCY ACT.

620 CHURCH STREET BUILDING CORPORATION,
ET AL.,
Petitioners,

vs.

WARNER G. BAIRD, ET AL.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

BRIEF AND ARGUMENT ON BEHALF OF PETITIONERS, EMIL ROSENTHAL AND B. K. GOODMAN, OWNERS OF SECOND AND THIRD MORTGAGES ON DEBTOR'S PROPERTY.

(Filed by Leave of Court)

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(Filed by Leave of Court)

STATEMENT OF THE CASE.

Because of the advancement of this case for argument, the usual time for filing complete briefs was not permitted. For the convenience of the court and in order that unnec-

essary reference to the short brief in support of the petition for certiorari may be avoided, the original position of petitioners will be herein restated, as well as petitioners' reply to the briefs of respondents. Thus the court will have the contentions of the petitioners under one cover.

The 620 Church Street Building Corporation (hereinafter referred to as Debtor) is a corporation organized under the laws of the State of Illinois. It owns a building in Evanston, Illinois, subject to three mortgages or trust deeds executed by it as follows:

1. First Mortgage dated June 30, 1928 securing bonds in the principal amount of	$445,000
2. Second mortgage dated July 13, 1928 securing notes in the principal amount of	40,250
3. Third mortgage dated June 3, 1931 securing notes in the principal amount of	27,000

The first mortgage bonds and the second mortgage notes were classified and allowed as classes 2, 3 and 4, respectively (R. 13).

The Debtor filed its voluntary petition for reorganization under Section 77B of the Bankruptcy Act on July 12, 1934. Prior to that time defaults had occurred on all of the above mortgages and foreclosure proceedings were pending in the State courts of Illinois. The District Court approved the petition as filed in good faith and all of the above mortgages were allowed as valid mortgages on the property of the Debtor.

A committee representing more than two-thirds of the bonds secured by the first mortgage filed a plan of reor-

ganization which provided that Debtor's property should be conveyed to the 636 Church Street Building Corporation, an Illinois corporation, not a party to the proceedings, having separate and independent stockholders and bondholders, but owning a building adjoining debtor's property. The consideration for this conveyance, under the plan, is to be $222,850 of first mortgage bonds (approximately 33% of total issue) and 25% of the capital stock of the grantee corporation. The plan provides that all such bonds and shares of stock shall be distributed to the first mortgage bondholders of Debtor and that no payment or consideration of any kind shall be given to the holders of the second and third mortgages or to the stockholders. The plan does not provide for a public sale of Debtor's property and gives no opportunity to the second and third mortgages to bid for the property on the same or better terms. It provides no method whereby the second and third mortgage holders may participate in the reorganization and, in a word, wipes out the liens and property rights of the second and third mortgagees.

The plan was accepted only by the committee in behalf of the holders of more than two-thirds of the first mortgage bonds. No acceptance was filed by the holders of the second mortgage or the third mortgage nor by any stockholder all of whom filed objections to the plan.

On March 31, 1936, the District Court entered an order confirming the plan. In the order of confirmation the Court found "that the principal property of the Debtor *has a fair market value* of $245,025 and that there is no equity over and above the $445,500" first mortgage bonds outstanding and "that the Debtor is accordingly insolvent."

The District Court further found that, "based on the evidence concerning the value" of the Debtor's property, "the court has appraised and does hereby appraise" the

claims of second and third mortgagees to be of no value, "there being no equity" in the Debtor's property over and above the first mortgage, and "accordingly no securities, cash or any other thing of value shall be distributed under the plan in respect of any claims" represented by the second and third mortgages "and the acceptance of the Plan by the holders of such claims is not a prerequisite to the confirmation of the Plan" (R. 15).

Questions Presented.

(1) Does Section 77B of the Bankruptcy Act authorize the District Court to approve a plan of reorganization which has not received the consent of two-thirds of each class of claims secured by junior liens, and which does not provide adequate protection for the payment of such claims?

(2) Are the rights of owners of junior liens acquired prior to the enactment of Section 77B of the Bankruptcy Act as Amended, including (a) the right to have the property subject to the junior liens sold at a public sale, and (b) the right to bid at such sale, and (c) the right to make redemption from a sale at the bid price in accordance with the Statutes of the State of Illinois, property rights, within the purview of the Fifth Amendment of the Constitution of the United States, of which the owners may not be divested without their consent?

SUMMARY OF THE ARGUMENT.

I.

The approval of a plan of reorganization by the District Court without the consent of the holders of two-thirds in amount of secured junior indebtednesses, without compensation to them and without making provision for their protection, is not authorized by Section 77B of the Bankruptcy Act, as amended.

A.

Section 77B requires the consent of two-thirds of any recognized class of creditors to a proposed plan of reorganization unless their claims are not affected or unless the plan makes provision for payment to them in full or unless the plan affords other adequate protection for the realization of the value of their interests, if such interests be affected.

Section 77B of the Bankruptcy Act, as amended.

B.

The methods prescribed by the Act for assuring such protection, so far as same are applicable to the instant case, are contained in sub-clauses (c) and (d) of Clause 5 of Subdivision B, which are as follows:

> Clause (c) By appraisal and payment in cash of the value of such claims or liens or, at objecting creditors' election, of the securities allotted to such interests under the plan.

Clause (d) By such method as will, in the opinion of the Judge, under and consistent with the circumstances in a particular case, equitably and fairly provide such protection.

C.

The method and manner of appraising securities held by secured creditors is provided in Section 57 h of the Bankruptcy Act, which is incorporated by express reference in Section 77B providing that the value of securities shall be determined by converting the same into money in one of the several ways indicated by said Section 57 h, as directed by the Court, and these are,

1. By converting the securities into money according to the terms of the agreement pursuant to which such securities were delivered to such creditors.

2. By agreement, arbitration or compromise between secured creditor and trustee in bankruptcy.

3. By litigation.

Section 57 h Bankruptcy Act: U. S. C. Title 11, Section 93, Clause h.

D.

The security of the second and third mortgages, in the instant case, were not evaluated or converted into money according to the terms of the Act.

The District Court appraised the property of the Debtor and from that appraisal concluded that there was no value in the second and third mortgages.

This action is clearly erroneous because the value of the second and third mortgage liens

of petitioners cannot be determined by the ability to collect against the proceeds of an immediate sale of the security.

E.

The plan of reorganization, in the instant case, is a plan in name only since the property which constituted the only asset of the Debtor was conveyed to an outside grantee, the entire consideration for the conveyance being conferred upon the first mortgage bondholders.

F.

If the lower courts be sustained, then first mortgages as well as junior mortgages may be found to have no value or some value less than the amount which the first mortgagees are willing to accept and hence first mortgagees like second mortgagees would be required to abide by a valuation of the security and forego the additional advantages which the mortgage confers.

This is the result which the Circuit Court of Appeals in the Tennessee Publishing Company case denied.

G.

It was not the legislative intent in enacting Section 77B to eliminate redemption and periods of grace.

II.

The rights of junior mortgage holders, acquired prior to the enactment of Section 77B, including the right to hold the mortgaged property (subject to the first mortgage) until the payment of the junior debt, the right to a public sale of the mortgaged property, the right to bid at such sale and the right to redeem after a sale are, under the law of the State of Illinois, substantive rights in specific property and the holders thereof cannot be deprived of them without their consent. If clauses (c) and (d) of subdivision (b) (5) are construed to authorize the destruction of such rights, they violate the Fifth Amendment to the Constitution of the United States.

A.

The rights of holders of second mortgages, like the rights of holders of first mortgages, become vested upon execution and delivery of the mortgage.

B.

The second mortgagee, like the first mortgagee, cannot be summarily divested of the rights procured under a second mortgage.

C.

The right of a junior mortgagee to redeem from a prior mortgage is distinct from, and in addition to his right to foreclose his mortgage.

Jones On Mortgages, 8th Edition, 1363.

D.

The Illinois statute on redemption provides that when any real estate is sold by virtue of an execution, judgment, decree of foreclosure, etc. any defendant or person interested in the premises, through or under the defendant, may redeem within twelve months from such sale by paying the sum for which the premises were sold with interest at 6% per annum. Creditors may redeem if redemption be not made by defendant or party claiming under or through him after the expiration of twelve months and within fifteen months after sale.

Chapter 77, Sections 16, 18 and 20, Illinois Revised Statutes 1931, Smith-Hurd.

E.

The second and third mortgagees, themselves possessing the right to retain their mortgages and the right to foreclose them, were forestalled in any attempt to realize upon their security and from exercising the right to redeem by the approval of the plan of reorganization which ordered the outright conveyance, for the benefit of the first mortgage bondholders, of the property constituting the security for the junior mortgages.

F.

It has been uniformly held that the right of redemption, as the same exists by law in the State of Illinois, is a substantial right constituting a rule of property.

Brine v. *Hartford Fire Insurance Company,* 96 U. S. 627, 636.

Parker v. *Dacres,* 130 U. S. 43, 48.

Fitch v. *Wetherbee,* 110 Ill. 475, 492.

Bronson v. *Kinzie,* 1 Howard, 311, 315.

Buszin v. *Martinowicz,* 178 Ill. App. 519, 523.

G.

The right to redeem being absolute and vested, it is not for the Court to put a price upon it or to declare it valueless.

Cram v. *Cottrell*, 48 Neb. 646.

In Re Georgian Hotel Corporation, 82 Fed. 2nd, 917, 920. (C. C. A. 7th).

H.

The cases cited by respondents in support of the proposition that junior mortgagees have no right to redeem unless the property is sold on foreclosure, do not support the contention, holding as they do, in substance, that it is the debtor's, and not the mortgagee's, right of redemption which may be disposed of in any proceeding which has for its object the liquidation of the debtor's liabilities.

Blair v. *Illinois Steel Co.*, 159 Ill., 350, 368.

American Mine and Equipment Co. v. *Illinois Coal Corporation*, 31 Fed. 2nd., 507, 511 and 512. (C. C. A. 7th)

Beet Growers Sugar Company v. *Columbia Trust Company*, 3 Fed. 2nd, 755, 757. (C. C. A. 9th)

I.

It is not true, as suggested in the respondents' briefs, that a Bankruptcy Court may order a sale free of liens, and thus free of the right to redeem when such sale will bring no more than the amount of the mortgage indebtedness.

Louisville Joint Stock Land Bank v. *Radford*, 295 U. S. 555, 584.

J.

A mortgage junior to a first mortgage confers upon the junior mortgagee the following substantive rights in the specific property described in the mortgage:

(1) The right to retain the lien until the indebtedness thereby secured is paid.

(2) The right to realize upon the security by a judicial public sale.

(3) The right to determine when such sale shall be held, subject to the discretion of the Court.

(4) The right to protect the interest of the junior mortgagee in the property by bidding at such sale whenever held and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt, either through receipt of the proceeds of a fair competitive sale, or by taking the property itself.

(5) The right to redeem from a prior mortgage.

K.

When the first mortgagee forecloses the only right which stands between the irrevocable loss by the junior mortgagee of his interest and the hope of salvaging it, is the right to redeem.

III.

Since the junior mortgagees possess rights in specific property of the Debtor, it is clear, under the doctrine of the Radford case, that they cannot be divested of them by subsequently enacted legislation.

Louisville Joint Stock Land Bank v. *Radford,* 295 U. S. 555, 589.

If Section 77B can be said to accomplish a divestiture of substantive rights in specific property, then it must be held to violate the Fifth Amendment of the Constitution of the United States.

Louisville Joint Stock Land Bank v. *Radford,* 295 U. S. 555, 589.

Conclusion.

To summarize, the Radford Case is decisive of the case at bar recognizing, as it does, the difference between the claims of general creditors and the claims of creditors holding substantive rights in specific property and holding that such substantive rights cannot be divested in the exercise of the bankruptcy power. Therefore, the following conclusions are irresistible:

(1) That a second mortgage does confer substantive rights in specific property.

(2) That Section 77B does not authorize a divestiture of those rights without consent.

(3) If the statute does permit such divestiture without consent of the holders of the second mortgage indebtedness, then it is unconstitutional.

ARGUMENT.

I.

The approval of the plan of reorganization by the District Court without the consent of the holders of two-thirds in amount of secured junior indebtednesses, without compensation to them and without making provision for their protection, is not authorized by Section 77B of the Bankruptcy Act, as amended.

The District Court and the Circuit Court of Appeals evidently assumed that clauses (c) and (d) of subdivision (b) (5) of Section 77B of the Bankruptcy Act authorizes the confirmation of a plan of reorganization without the consent of junior lienholders and without paying any money or other thing of value for the liens. It must be admitted that there is some ground for this assumption in the language used, but as this assumption wipes out certain rights of junior lienors for many years considered and dealt with as valuable and vested, substantive rights in specific property, on the bases of which millions of dollars have been invested in junior mortgages by private and public institutions, it should not be entertained unless the language used leaves no alternative. A timely example of such public investments are the second mortgages by Federal Farm Loan Banks, the purpose of which is to give relief during the depression.

Let us examine the applicable provisions of Section 77B. They are found in subdivision (b), clauses (1) and (5). It is necessary, however, to read in connection therewith the entire subdivision and, as well, the section of the gen-

eral Bankruptcy Act (Section 57 (h)) therein specifically incorporated. The assumption of the courts below appears justified only if regard is had to sub-clauses (c) and (d) of clause (5) of subsection (b), and even then some of the words used must be given an unusual meaning. The provisions of subsection (b), clauses (1) and (5) pertinent to the case at bar, together with clause (h) of Section 57 of the Bankruptcy Act (Section 93 (h) of the United States Code Annotated, Title 11) referred to therein are as follows:*

> "A plan of reorganization within the meaning of this Section shall include provisions for modifying or altering the rights of creditors generally, or any class of them, secured or unsecured, either *through the issuance of new securities* • • • or otherwise; (Subsection (b), clause (1)) • • • shall provide in respect of each class of creditors of which less than two-thirds in amount shall accept such plan • • • adequate protection for the realization by them of the *value of their interests, claims or liens* • • • (Subsection (b), clause (5))
>
> (c) By *appraisal and payment in cash of the value of such interests, claims or liens,* • • • or
>
> (d) By such method as will in the opinion of the judge • • • *equitably and fairly provide such protection* • • • (Subclauses (a) and (b) of clause (5) of subsection (b)) (Italics ours)

Subsection (b), toward its conclusion (about eighteen lines from the end of the subsection) provides:

> "In case of secured claims entitled to the provisions of clause (5) of this subdivision (b), the

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*The entire subdivision is given in appendix A of this brief.

> value of the security shall be determined in the manner provided in Section 93, clause (h) of this title (Section 57 (h) of the Bankruptcy Act) and if the amount of such value shall be less than the amount of the claim, the excess may be classified as an unsecured claim."

The section of the Bankruptcy Law as existing at the time of the passage of Section 77B—Section 57 (h) aforesaid—thus incorporated by express reference, provides:

> "The value of securities held by secured creditors shall be determined by converting the same into money according to *the terms of the agreement pursuant to which such securities were delivered to such creditors* or by such creditors and the trustee, by agreement, arbitration, compromise, or litigation, as the court may direct, and the amount of such value shall be credited upon such claims, and a dividend shall be paid only on the unpaid balance." (Italics ours.)

The above provisions authorize the approval of a plan without the consent of the lien creditors, but the passages in italics clearly require *the issuance of new securities* or protection for the realization by the nonconsenting lienholders of the *value of their interests, claims or liens.* Surely it does violence to the italicized words to confirm a plan which contemplates the issuance of no new securities and which expressly excludes payment and the delivery of anything of value to the lienholders.

While clause (c) expressly authorizes appraisal and payment of claims of nonconsenting lienholders, the later language of the Act with equal definiteness states that in the case of secured claims the value of the security shall be ascertained as provided in Section 57 (h) of the Bankruptcy Act. (Section 93 (h), Title 11, United States Code

Annotated.) Section 57 (h) expressly provides, as one of the methods of ascertaining the value of secured claims, the method provided by the contract under which the security was given. Therefore, in the case of a mortgage, the value may be ascertained by foreclosure proceedings.

It is submitted that if regard is had to the entire subdivision (b) (5) of section 77B and to section 57 (h) of the Bankruptcy Act, there is no clear and unequivocal authority for the order entered by the District Court. In the absence of such clear and unequivocal language, an interpretation which vitiates claims secured by liens long regarded as substantive rights in specific property should not be countenanced.

Clause (c) of subdivision (b) (5) expressly provides for an appraisal of the *value of such interests, claims or liens* but the order of the District Court specifically states that the Court based its appraisal on the evidence of the "*fair market value of the principal property of the Debtor.*" This is clearly erroneous as other factors necessarily enter into the value of liens. The present fair market value of the principal property of the Debtor, if it can be said to have a "market," may (owing to temporary causes such as the widespread depression, the large amount of such property on the market, the temporary shortage of money available for investment in real estate) be very low, but the liens, because they may be enforced against the property and because they may enable the owners to redeem from a sale twelve months thereafter, may be very valuable. The Courts below ignored all these factors.

It may be pertinently inquired, is the plan a plan of reorganization in the sense contemplated by Section 77B? It is called a plan but it is one only in name. The substance of it is the appropriation of the property for the

benefit of the first mortgage bondholders. The Debtor's property is conveyed for certain stocks and bonds of an unknown value, not ascertainable in money, certainly not of a value declared by the Court. For all that appears in the proceedings, the value of the stocks and bonds distributed to the first mortgage bondholders may be worth far more than the amount due them. Such excess, if any, belongs to the junior mortgagees and stockholders. On the other hand, the value of the stocks and bonds issued for Debtor's property may be very low. If the latter is true, why should not the junior lienholders and stockholders, rather than an outsider, be given the opportunity to acquire the property for the low price? Can a plan be called a plan of reorganization which appropriates the property of the Debtor for the benefit of an outside party and distributes a consideration of an unknown value to the first lien creditors? It would seem that if the court were empowered to appraise the value of Debtor's property for the purpose of a plan, then it was only fair to provide for the realization by the junior lienors and stockholders of their interests and claims in the property by giving to them the opportunity to acquire the property at the amount found by the court as the value thereof, namely, $245,025.

Petitioners respectfully urge that what the court authorized is not a genuine plan of reorganization as contemplated by Section 77B. This law was passed by Congress to benefit distressed debtors and creditors alike. All that was done here was that the property of the Debtor was taken for the benefit of a stranger and the first mortgage bondholders to the detriment of the Debtor and second and third mortgage holders.

If the clauses (c) and (d) of subdivision (b) (5) be construed to authorize the consummation of a plan without the consent of an entire class of secured creditors, by

appraising the property of the Debtor at an hypothetical market value, and summarily eliminating a class of secured creditors, if based upon such hypothetical market value of the property, the claims of such secured creditors are given no value, or by paying to such classes of secured creditors the value indicated by the hypothetical market value of the property, then it would inevitably follow that all mortgages, first mortgage as well as junior mortgages, might be found to have no value or only a nominal value because of temporarily depressed conditions, and as a result all mortgages might be effectually barred from participating to the full extent of their substantive rights in specific property. This would enable the Debtor to eliminate all its creditors without their consent and over their objections and carry out a plan of reorganization which would permit the Debtor to keep the property, free of all liens, and alone receive all of the increments and advantages of the increased values of a not distant future. This is exactly the position of the parties in the *Tennessee Publishing Co.* case, which was argued immediately preceding the argument of the instant case. The Congress, it is submitted, did not intend this result and the respondents representing the first mortgage bondholders would be the loudest complainers if the first mortgage holders were treated in this case as were the holders of the second and third mortgages.

No extended argument is necessary to show that the rights of first mortgage bondholders are, in principle, the same as the rights of second mortgage holders. Each class has, on default, among other rights, the title to the property as security for the payment of the debt, the right to foreclose, the right to sell the property at a public sale and the right to bid at the sale. It is true that the junior lienors have all these rights subject to the claim of the first mortgage, but otherwise the rights are identical.

What the law aims to bring about is an opportunity for debtors and creditors to get together and agree on plans of reorganization agreeable to all or at least to a substantial majority of each class of creditors—each yielding something for the sake of harmony and self-interest, along the lines of compositions in bankruptcy. Such agreements have long been authorized by bankruptcy laws in respect of unsecured claims and such laws have uniformly been held valid. Section 77B extends the principle to secured claims and if the law is to be sustained, it must be upon the ground that a plan of reorganization thereunder is merely an agreement between the debtor and all classes of secured creditors with the will of substantial majorities in each class imposed on their respective minorities.

It may be urged that if the consent of each class of creditors is required, the usefulness of the law will be impaired if not wholly obstructed. Particularly, say respondents, will this be the case if the consent of junior lienholders is required. Experience alone can determine this. In the meantime, it may be safely asserted that many plans have been confirmed with the consent of all classes of creditors in proceedings under Section 77B of the Act in the two years in which that Section has been in effect, and particularly has this been the case in England and in the Dominion of Canada where similar laws have been in effect for many years.

On the other hand, petitioners urge that the law will be well nigh useless if debtors and junior lienors are deterred from seeking reorganization under Section 77B for fear that they will lose all their rights through the insistence of the holders of the first mortgage that the debtor's property has a present and temporary market value of less than the amount of the first mortgage which in these times is generally true. If the order of the Dis-

trict Court in this case is allowed to stand by this Court, then under that high sanction, the attitude of the senior security holders will be always one of demanding everything for themselves and giving nothing to debtors and creditors junior to them, while, on the contrary, if petitioners be sustained a more humane attitude of "give and take" will develop which will bring about more harmonious relations between all parties and redound not only to their advantage but to the economic welfare of the nation as a whole. Such, it is earnestly urged, more nearly squares with the probable legislative intent.

Considering the arduous conditions which affected the nation when Section 77B was enacted, it is impossible to believe that Congress intended to eliminate grace periods when periods of grace were so necessary—so necessary, indeed, that moratoria in foreclosures were the legal vogue.

Subdivision (f) of Section 77B of the Bankruptcy Act provides that the Judge shall not confirm a plan unless satisfied that "(1) it is fair and reasonable and does not discriminate unfairly in favor of any class of creditors."

As has been said, the plan in this case deprives the Debtor of all of its property and gives the proceeds thereof only to the first mortgage bondholders, nothing to the second and third mortgage holders or to the stockholders. It is difficult to see how any plan that provides solely for one class of creditors to the absolute exclusion of all other creditors can be a fair plan. It would not even be a fair foreclosure, cutting out, as it does, the right of redemption. The junior creditors were denied even the opportunity of sharing any future increases in value by a conveyance of the property to a stranger, the 636 Church Street Building Corporation. By this conveyance, the loss of the junior lienholders and stockholders was made complete and ir-

revocable. A clearer case of "unfair discrimination in favor of a class of creditors" can hardly be imagined.

Counsel for respondents lay stress on the fact that the court found the value of the property to be less than the amount of the first mortgage. It should, however, be remembered that what the court found was the supposed, fair market value of the property. This necessarily meant the fair market value at the time of the proceedings. The court will take judicial notice of the fact that the nation has gone through a widespread depression, which has temporarily affected all values and particularly the market value of real estate. To take a well known example, the United States Steel Corporation incurred deficits running into millions in recent years. Its common stock sold as low as $25.00 per share only two or three years ago. Today, the common stock is selling at about $75.00 per share, an increase of 200% and it is not at all beyond the realms of possibility that the stock will soon sell at the price prevailing in 1929 when the stock was selling at about $190.00 per share.

The same factors which cause prices of stocks and commodities to rise and fall, operate upon real estate. While the tempo of the price movement of real estate is slower, there can be no denial that it is inevitably affected by general upward and downward trends.

Finally, on this point, petitioners paraphrase a statement recently made by an eminent jurist, namely:

> A plan of reorganization should mean an honest desire to save a Debtor and its creditors from liquidation, keep the Debtor as a going concern, save whatever value there may be in it as a going concern distinguished from a liquidating concern.

Surely nothing can be further from this description than the plan confirmed by the District Court in this case.

For many years junior securities have constituted an important element in financial transactions. Undoubtedly an investor in a junior mortgage is influenced in making his investment by the fact (1) that in the event there should be a default in the payment of his indebtedness he would have the right and the opportunity to foreclose his mortgage and offer the mortgaged property for sale, subject to the prior lien, and (2) that should there be a default in payment of the first mortgage indebtedness, his rights may not be immediately taken away, but that it would be necessary for the first mortgagee to file foreclosure proceedings and if the property does not sell for enough to pay both the first and second mortgages in full, then he would have a period of at least 12 months after the sale to redeem.

II.

The rights of junior mortgage holders, acquired prior to the enactment of Section 77B, including the right to hold the mortgaged property (subject to the first mortgage) until the payment of the junior debt, the right to a public sale of the mortgaged property, the right to bid at such sale and the right to redeem after a sale are, under the law of the State of Illinois, substantive rights in specific property and the holders thereof cannot be deprived of them without their consent. If clauses (c) and (d) of subdivision (b) (5) are construed to authorize the destruction of such rights, they violate the Fifth Amendment to the Constitution of the United States.

The rights of the holders of mortgages, whether first or second, become vested on the execution and delivery of the

mortgages under laws then in existence. In Illinois, upon the execution of a mortgage and before default, the mortgagee is invested with a base or determinable fee title to the mortgaged property. He cannot be divested of this title except by payment in full.

After default, the mortgagee becomes the owner of the mortgaged property subject to the right of redemption. He may bring ejectment against the mortgagor and those claiming under him and exercise all the rights of ownership.

Jones on Mortgages, 8th Edition, Sec. 29.

Lightcap v. *Bradley,* 186 Illinois 510.

Bradley v. *Lightcap,* 195 U. S. 1.

Under the terms of the mortgage, the mortgagee may, on default, proceed to foreclose his lien and in such proceedings obtain a public sale of the property. He has the right to bid at such sale. A junior mortgagee, of course, sells subject to the prior mortgage.

A junior mortgagee has the right to redeem from a prior mortgage at any time after the maturity of the prior mortgage. This right to redeem is distinct from his right to foreclose his mortgage. The right of a junior mortgagee to redeem, says Jones on Mortgages, (8th ed.) section 1363, is a common law right and is entirely independent of the right of redemption given to creditors. The language of most of the cases is broad enough to establish the doctrine that a junior mortgagee has, under all circumstances, the absolute right to pay off, or redeem from, a senior mortgage, past due.

The redemption provisions of the Illinois Statute, as the same existed and were in force at the time of the execution and delivery of the mortgage indebtedness in question,

are contained in Chapter 77 of the Illinois Revised Statutes for 1931 (Smith-Hurd).

Section 16 provides that when any real estate is sold by virtue of an execution, judgment or decree of foreclosure, or enforcement of any mechanic's lien or vendor's lien, or for the payment of money, it shall be the duty of the sheriff, master in chancery or other officer, to give to the purchaser a certificate describing the premises purchased, showing the amount paid, the name of the person in whose favor the execution or decree stands, the amount of the bid and the time when the purchaser will be entitled to a deed, unless the premises be redeemed.

Section 18 of the statute provides that any defendant or any person interested in the premises through or under the defendant may redeem within twelve months from such sale by paying that sum of money for which the premises were sold, with interest at the rate of 6% per annum from the time of such sale. Upon such payment the sale and certificate shall be null and void.

Section 20 of the Act provides for redemption by creditors and states that if redemption is not made by a party entitled to redeem under Section 18 then, after the expiration of twelve months, and within fifteen months after the sale, such creditor may redeem.*

In *Brine* v. *The Hartford Fire Insurance Company,* 96 U. S. 627, this court distinctly held that the statute of Illinois which so allowed redemption confers a substantial right and thereby becomes a rule of property. The court said at page 636:

> "The Legislature of Illinois has prescribed, as an essential element of the transfer by the courts in foreclosure suits, that there shall remain to the mortgagor

*Sections 16, 18 and 20 of the Illinois Redemption Act appear in full hereinafter in appendix B.

> the right of redemption for twelve months, and to judgment creditors a similar right for fifteen months, after the sale, before the right of the purchaser to the title becomes vested. This right, as a condition on which the title passes, is as obligatory on the Federal courts as on the State Courts, because in both cases it is made a rule of property by the Legislature, which had the power to prescribe such a rule. • • • But there is another view of the question which is equally forcible, and which leads to the same result. All contracts between private parties are made with reference to the law of the place where they are made or are to be performed. Their construction, validity and effect are governed by the place where they are made and are to be performed, if that be the same as it is in this case. It is, therefore, said that these laws enter into and become a part of the contract."

Again, in *Parker* v. *Dacres,* 130 U. S. 43, Mr. Justice Harlan, delivering an opinion of this court, said at page 48:

> "In many of the states the right to redeem within a prescribed time after sale under a decree of foreclosure is given, in certain cases, by statute. This right, when thus given, is a substantial one, to be recognized even in the Courts of the United States sitting in equity, because the statute constitutes a rule of property in the State that enacts it. *Brine* v. *Hartford F. Ins. Co.,* 96 U. S. 627; *Hammock* v. *Farmers Loan & T. Co.,* 105 U. S. 77; 88 *Mason* v. *Northwestern Mut. L. Ins. Co.,* 106 U. S. 164; *Conn. Mut. L. Ins. Co.* v. *Cushman,* 108 U. S. 51, 63."

The Supreme Court of Illinois has repeatedly confirmed the statute of redemption of its own state. Thus in *Fitch* v. *Wetherbee,* 110 Ill. 475, the court in commenting upon

the absoluteness of the right of redemption, said at page 492:

> "The right of redemption given by the statute to a decree or judgment creditor is not affected by a failure of the court to provide in its decree for the sale of real estate, with the privilege of redemption. It is the statute that gives the right of redemption, and not the decree of the court. In a case where the statute authorizes a redemption from a sale, a clause in the decree ordering the sale that declares the sale shall be absolute, will not bar that right. That portion of the decree will be regarded as inoperative, and a redemption will be allowed as in other cases. Nor does it make any difference whether the sale was conducted by an officer of the law or by one appointed by the court to perform that special duty."

Other illuminating cases upon the subject are:

Bronson v. *Kinzie*, 1 How. 311, 315.
Buszin v. *Martinowicz*, 178 Ill. App. 519, 523.
Turk v. *Mayberry*, 121 Pac. 665, 669 (Okla. 1912).

The right to redeem by paying the price bid at the foreclosure sale, continuing as it does for 12, and if judgment be obtained, for 15 months, gives to junior security holders a valuable option. Frequently the first mortgagee is the successful bidder, and, as frequently, he bids less than the amount of the indebtedness, as is evidenced by the well nigh invariable practice of taking deficiency decrees. Particularly valuable is the right of redemption in a rising market. Whether valuable or not from a monetary standpoint, however, it is absolute and vested and it is not for the court to put a price upon it or to declare it valueless. As was said in *Cram* v. *Cottrell*, 48 Neb. 646:

> "The plaintiffs had a legal right to redeem, whether or not the exercise of that right would be profitable to

them. It was for them to determine whether they should exercise the right, and not for the court to deny them the right because, in its opinion, its exercise would not be profitable."

The Circuit Court of Appeals for the Seventh Circuit, *In re Georgian Hotel Corporation*, 82 Fed. (2nd) 917, recognized that the right of subordinate creditors to redeem should be observed by the court, saying at page 920:

> "While it is not likely that at the present time the subordinate creditors would have realized anything if the first mortgage had been foreclosed, these creditors would, for three months after one year following the foreclosure sale, have had a right of redemption—a right which might have been valuable. And there is the possibility that, with a substantial 'comeback' in affairs, property values may increase sufficiently to give the debtor a substantial equity in the property of which these creditors would have the benefit."

Counsel for the first mortgage bondholders committee deny that junior mortgagees have the right to redeem in Illinois except when mortgaged property is sold on foreclosure, and they rely upon

Blair v. *Illinois Steel Co.*, 159 Illinois 350.
American Mine Equipment Co. v. *Illinois Coal Corporation*, 31 Fed. (2nd) 507.
Beet Growers Sugar Co. v. *Columbia Trust Co.*, 3 Fed. (2nd) 755.

An examination of the above and other cases cited by counsel for the first mortgage bondholders committee shows that they were led astray by confusing the equity of redemption or right to redeem possessed by a corporation which is the subject of dissolution, general equity receivership or bankruptcy proceedings, and the right to redeem

possessed by a solvent holder of a junior mortgage in no manner involved in a proceeding looking to the distribution of its assets to its creditors.

Certainly the equity of redemption or the right to redeem is a property right and is an asset. If, therefore, the owner thereof be in some legal process of liquidation, then its equity of redemption or right to redeem may be disposed of exactly in the same manner as any other asset may be disposed of in such proceedings. No debtor has the right to retain any property not expressly exempted by law when involved in any kind of legal liquidation. The question, however, is somewhat academic because the instant case is not one of a general equity receivership nor is it a dissolution under state statute. The case arises out of a petition for reorganization filed under Section 77B of the Bankruptcy Act as amended. The affairs, assets and indebtednesses of the Debtor only are involved. The holders of junior liens are not connected with the proceedings except as claimants.

It is true that the Bankruptcy Court may order a sale of the property of the bankrupt free of liens, the liens to attach to the proceeds of the sale. Even this was not done in the case at bar. If a sale free of liens had been ordered, the second and third mortgagees would have had an opportunity to protect their liens by bidding at the sale. Even if the order had been to transfer the property for the stocks and bonds of the 636 Church Street Building Corporation and the liens attached to these bonds and stocks as constituting the proceeds of the sale, then the second and third mortgages would have had a lien thereon, there being nothing in the record to show the value of the stocks and bonds.

It is well established that the Bankruptcy Court may order a sale free of liens only in a proper case where some bene-

fit will be derived by the bankrupt estate, where the delays and expense incident to a foreclosure proceeding may be avoided in the interests of prompt liquidation and where something will be left for distribution to general creditors after satisfying liens upon the property so sold. In no case, however, should a bankruptcy court order such a sale when it is evident that the price which may be expected will be less than the mortgages or other liens upon the property.

This court has spoken with finality on this subject in the *Radford* case where at page 584 Justice Brandeis, in speaking of the sale of the property of the bankrupt, free of encumbrance and transferring the rights of lienholders to the proceeds of the sale, said:

> "But there had been no suggestion that such a sale could be made to the prejudice of the lienor, in the interest of either the debtor or of other creditors. By the settled practice, a sale free of liens will not be ordered by the bankruptcy court if it appears that the amount of the encumbrance exceeds the value of the property. And the sale is always made so as to obtain for the property the highest possible price. No court appears ever to have authorized a sale at a price less than that which the lien creditor offered to pay for the property in cash. Thus, a sale free of liens in no way impairs any substantive right of the mortgage (mortgagee)."

A quick survey of the cases relied upon by adversary counsel will demonstrate their utter inapplicability.

In *Blair* v. *Illinois Steel Co.*, 159 Ill. 350 (Brief of Chester R. Davis, *et al.* page 19), a bill was filed by a judgment creditor alleging the insolvency of the Joliet Enterprise Corporation, praying for the appointment of a receiver,

the dissolution of the corporation and the enforcement of the individual liabilities of the stockholders and directors. A cross-bill was filed in the case by Blair and some of the beneficiaries named in the trust deed in which Blair was Trustee, to foreclose a trust deed which had been executed by the debtor to secure the claims of certain creditors. This cross-bill and the trust deed involved therein were attacked upon the ground that the trust deed constituted an unlawful attempt to prefer creditors.

A receiver was appointed. The debtor corporation defaulted on the bill to dissolve but answered contesting the cross-bills of various creditors in which attack was made upon the trust deed and the bill to foreclose the same. The Illinois Steel Co., together with the Cleveland Rolling Mill Co., answered the cross-bill to foreclose challenging the validity of the trust deed. The trial court held the trust deed to be an unlawful preference and dismissed the cross-bill to foreclose it. On appeal to the Appellate Court the judgment of the trial court was affirmed, whereupon an appeal was taken to the Supreme Court of Illinois.

It is important to observe that the Supreme Court of Illinois rendered two opinions, one upon the original hearing and one upon rehearing. An examination of the briefs of both sides reveals that the question of the propriety of a sale eliminating the right of redemption was not presented. In its first opinion the court did state that in a proceeding under the winding-up statute, which had for its purpose the dissolution of an insolvent corporation and closing up its business and affairs, it was proper to order a sale free of redemption. In this connection it is vital to note that the redemption spoken of was the right of redemption of the corporate debtor which was being dissolved in a proceeding in which its assets were being collected and used in payment of its debts.

Upon rehearing, however, the court decided the only question before it, which concerned merely the validity of the trust deed, and, in so deciding, the court overruled the decree of the courts below in dismissing the cross-bill, held that said decrees were erroneous and remanded the case with instructions to enter a decree in conformity with the prayer of the bill. The language of the Supreme Court of Illinois in thus allowing the foreclosure of the trust deed by the Trustee named therein, the foreclosure to be conducted in the very proceedings originally instituted to dissolve the corporation, is as follows (page 368):

> "We think the decree of the court below in dismissing the cross-blll of appellants was erroneous and should be reversed. The cause will be remanded with instructions to it to enter a decree in conformity with the prayer of that bill."

It is thus apparent that in the opinion on rehearing which actually decided the litigation, there is no mention of a receiver's sale or the right of redemption. The language of the court in its original opinion, respecting sales free of redemption, in view of the decision on rehearing, becomes purely *obiter dictum*. To repeat, even in this dictum the court had in mind only the right of redemption of the debtor itself.

It is the *Blair* case which our learned opponents rely upon as establishing the law to the effect that the right of junior mortgagees to redeem may be obliterated by a receivership sale of encumbered property of the debtor. The *Blair* case constitutes the foundation stone upon which rests one of the main contentions of our adversaries. The *Blair* case being wholly inapplicable, the entire structure of the argument superimposed thereon, falls.

In *American Mine Equipment Company* v. *Illinois Coal Corporation*, 31 Fed. (2nd) 507 (C. C. A. 7th, 1929) (Brief of Chester R. Davis, *et al.*, page 20) a simple contract creditor filed its so-called "general creditor's bill" asking that the court enforce its claim, determine the claims of all other creditors of the Coal Company, marshal the assets and sell and distribute the same among the creditors in accordance with their respective rights. The bill prayed for the appointment of a receiver to take possession of the property and to operate it. The bill also prayed that if it be found to the best interests of the creditors the property should be sold in whole or in part with provision to be made for the preservation of all equities and priorities among the creditors and that the property be sold either subject to, or free and clear from, liens and encumbrances as the court might direct.

The debtor corporation in its answer admitted all of the important allegations of the bill and consented to the appointment of a receiver.

Two days after the filing of the original bill two bills for the foreclosure of separate mortgages upon the debtor's property were filed and consolidated with the original bill of complaint, and the receiver was directed to act as receiver in the consolidated cause. After two years had elapsed during which receivership certificates in an important amount had been authorized and sold, the receiver petitioned the court recommending a sale free of all liens and free of the right of redemption. Thereupon the debtor denied the jurisdiction of the court to deprive it of a statutory right, denied its insolvency and agreed to waive its right of redemption only if a plan of reorganization were adopted recognizing the company's stockholders. The court made a finding of insolvency and authorized the sale as prayed for in the petition holding that such a sale was not

made under a decree of foreclosure. Nowhere in the opinion, however, is there any indication that the mortgagees were denied any priority to which their respective contracts entitled them. The equity of redemption involved was, as in the *Blair* case, the equity of redemption of the debtor. This is distinctly recognized by the court in its opinion when it says at page 512:

> "The equity of redemption was property; and by this voluntary consent to the general administration of all *its* property, and the turning over of all of it to the receiver, *to whose authority the defendant's consent was indispensable,* the defendant in the action conveyed this as well as all its other property, and the court could then direct its disposition with the other property conveyed."

In point of fact the *American Equipment Company* case actually supports petitioners' position. The court particularly noticed *that the mortgagee in that case consented to the sale* by the receiver free of redemption. The court said at page 511:

> "* * * when appellant definitely consented that the property might be sold by the receiver free of the mortgage and other liens, and that thereupon the mortgage and other liens attach only to the proceeds, in our judgment it amounted to a waiver or conveyance of the right of redemption as effectually as if one holding an equity in mortgaged property deeded it to a third person with power to sell it and make title to the purchaser, and satisfy the mortgage out of the proceeds. *Surely this is so if, as was here the case, the mortgagee consents to this arrangement;* for thereby he waives the lien of his mortgage on the property itself, making it impossible for him thereafter to fore-

close, and substitutes therefor a claim upon the proceeds, in respect to which no statutory redemption is provided."

It may be mentioned in passing that the court in the *American Mine Equipment* case relies upon the case of *Blair* v. *Illinois Steel Company* without noticing that the language of the *Blair* case used as authority did not constitute any proper part of the decision as that case was finally determined.

In *Beet Growers Sugar Company* v. *Columbia Trust Company*, 3 Fed. (2nd) 755 (C. C. A. 9th, 1925) (Brief of Chester R. Davis, *et al.*, page 20) the Circuit Court of Appeals of the Ninth Circuit had before it, as did the courts in the two preceding cases, a consideration of the equity of redemption or right to redeem of the debtor itself. In that case an original bill was filed to foreclose a trust deed and a receiver was appointed. Thereafter one of the holders of preferred stock of the company intervened and *with the consent of the corporate debtor* the receivership was converted into a general receivership to determine the rights of all parties to the suit and to wind up the affairs of the corporation. As is observed in the opinion of the court (page 757):

> "To this procedure the appellant consented and it made no objection to the allowance of the order for the enlargement of the powers of the receiver. * * * In so assenting it must be held to have subjected itself to the orders and judgment of the court in the exercise of all of its inherent powers in a receivership case."

Thus, all that is involved in this decision is a sale of the right to redeem *of the debtor* by a receiver who, with the debtor's consent, obtained, by order of court, the enlarged

powers of a general receivership. It is accordingly apparent that the decision has no bearing upon the right to redeem of the holder of a junior encumbrance.

The Court will remember that the District Court in this case did not order a public sale of the property, but confirmed a plan which provided that the property should be sold to a private corporation for a consideration payable in stock and bonds, the value of which depended on other property owned by the grantee corporation and was not ascertained in any manner. The plan did not afford any opportunity to the Debtor or to the junior lienholders to bid for the property and the character of the consideration given by the grantee corporation for the conveyance of the property was such as to preclude any such opportunity.

However, the right of the second and third mortgagees to redeem, is not the only right of which they were deprived. They have other rights under their respective mortgages and on this matter too, this Court has spoken in the *Radford* case.

The right of a mortgagee to insist upon full payment before giving up his security has always been regarded as the essence of a mortgage. This right inheres in a mortgage whether it be a first or a second encumbrance. The only difference between the two is that the second mortgagee may be deprived of his right to subject the property to the payment of his claim by a foreclosure by the first mortgagee. Under the laws of Illinois, when such an event occurs, the second mortgagee has the right to bid at such sale in order to protect his lien and if he is not the successful bidder he has the right to redeem the property from the sale under the first mortgage at the price bid therefor. This right runs for a period of twelve months from the date of the sale. If the first mortgagee does not pursue

his remedy by foreclosure, the right to redeem would continue until all rights under the mortgage would expire under the Statute of Limitations, which in the State of Illinois, is 20 years.

The Radford decision clearly establishes that a mortgagee has the following rights:

(1) The right to retain the lien until the indebtedness thereby secured is paid.

(2) The right to realize upon the security by a judicial public sale.

(3) The right to determine when such sale shall be held, subject only to the discretion of the court.

(4) The right to protect its interest in the property by bidding at such sale whenever held, and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt, either through receipt of the proceeds of a fair competitive sale or by taking the property itself.

A first mortgage was involved in the *Radford* case. A second mortgagee has the same rights. The only difference is that these rights are subject to the prior payment of the first mortgage.

A second mortgagee has an additional right as before pointed out, namely the right to redeem the property in case it is sold to satisfy a prior lien. This right to redeem, extending as it does into the future for a period of 12 to 15 months, gives to a second mortgagee a valuable option to purchase the property at the price bid at the sale, which generally is much less than the indebtedness due under the first mortgage.

If clauses (c) and (d) of subdivision (b) (5) of Section 77B be construed as authorizing the erasure of rights

of second and third mortgagees without their consent and without compensation or protection, then, in principle, the rights of first mortgagees may be similarly and without their consent adversely affected. While the rights of holders of junior securities are subject to the prior payment of the indebtedness of a senior lien, such holders of junior securities, nevertheless, possess rights which are in no manner eliminated by the presence of a prior lien. A first mortgagee cannot object to the request of a junior mortgagee to have a public sale, nor can such first mortgagee deny the right to a junior creditor to bid at the sale. Certainly the important right to redeem becomes solidified when the foreclosure by first mortgagee reaches the final stage of a sale.

When a second mortgagee is confronted by a foreclosure of the first mortgage and is unsuccessful in bidding, or is unable to bid at the foreclosure sale, he has one right which stands between the immediate irrevocable loss of his interest and the hope of salvaging it. This right is the right to redeem. It is the very existence of the senior lien and the capacity of the first mortgagee to foreclose it that makes the equity or right of redemption so necessary to the junior lienholder, since it is only by redemption that he can enforce his claim upon the security.

The substantive right in specific property held by the second mortgagee does not depend for its existence upon any priorities in remedies. Although a second mortgage is subject to the first in point of opportunity to receive payment it is dependent upon nothing but its own existence for its own attributes of property and security. When the mortgagor executes and delivers the second mortgage to a creditor, a substantive right in specific property is created and it is as inviolable within its own limits as a first mortgage and, as has been heretofore said, it does

not appear and vanish with the rise and fall of the market.

To deny to whole classes of secured creditors rights which are not in any manner affected by the presence of a senior mortgage and to hold that the clauses of Section 77B before mentioned permit such denial, is to give to those provisions an unconstitutional interpretation.

It is contended by our learned adversaries that:

> "Granted that petitioners' redemption rights were vested property rights under the laws of Illinois, such property rights were subject to be divested as an incident to the exercise of bankruptcy power."

It is at this point that we must carefully take our bearings using the *Radford* case as a chart. There is a difference between simple contract claims against the debtor personally which, it has long been held, may be scaled down and even discharged in the exercise of the bankruptcy power and claims secured by a lien on specific property. There is a sharp difference between a right existing by way of an unsecured claim against the debtor, as to which all general creditors stand upon the same footing, and a creditor who, by virtue of contract and conveyance holds, in addition to his claim *in personam*, an interest in specific property. This difference is clearly perceived and emphatically announced in the *Radford* case which, by its timely pronouncement, will enable some drifting courts to get back to their moorings where they can tie to tested principles of substantive law.

By all processes of logical reasoning, this court, in the *Radford* case, rendered an opinion, the inevitable result of which is to confirm the contentions here made. There this court held the Frazier-Lemke Act unconstitutional be-

cause it proposed to deny property rights under a mortgage existing prior to the enactment of the Statute. At page 589 the court said:

> "Because the act is retroactive in terms and as here applied purports to take away rights of the mortgagee in specific property, another provision of the Constitution is controlling. * * *
>
> "The Bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment. * * *
>
> "But the effect of the act here complained of * * * is the taking of substantive rights in specific property acquired * * * prior to the Act."

Unless it is possible to say, therefore, that the rights of junior security holders are dependent wholly upon a temporary value based upon opinion and found by the court and unless the substantive, although not monetary, rights to require a public sale, to be permitted to bid thereat, and to redeem, are regarded as of no legal significance, it must follow with mathematical inevitability that any attempt to disregard and destroy such rights is an invalid exercise of governmental power. If a statute makes such attempt it is unconstitutional, and if a court by its order produces the same result under a statute which does not authorize it, its order is invalid. In the one case it is a legislative, and in the other a judicial, invasion of private rights.

Because the rights above enumerated, that is, the right to retain the lien until the indebtedness is paid, the right to a judicial public sale, the right to bid at the sale and the right to redeem, are substantive rights in specific property and since all of these rights were disregarded by the order of the District Court, which approved the plan of reorganization, it necessarily follows that the order of the

District Court is invalid because thereby the petitioners were deprived of their property in violation of the 5th Amendment of the Constitution of the United States. If the order is invalid, the Circuit Court of Appeals should have allowed the appeal and should have set the order aside. If clauses (c) and (d) of Subdivision (b) (5) authorize such an order, then clauses (c) and (d) are violative of the 5th Amendment of the Constitution of the United States.

Respondents insist that the holders of the second and third mortgages have not been deprived of substantive rights in specific property because the court found that their claims, interests and liens were of no value; that the Plan afforded "adequate protection" but that such "adequate protection" yielded nothing because the value of the property of the Debtor, as found by the court, was not sufficient to pay the first mortgagee in full. They rely on the opinion of the Circuit Court of Appeals for the Fourth Circuit in *Campbell* v. *Alleghany Corporation,* 75 Fed. (2nd) 947, pages 953-954, from which they quote extensively. We wish to point out, however, that in the case of *Campbell* v. *Alleghany Corporation, two-thirds of each class of creditors consented.* The court used the following language:

> "We do not think that the requirement that secured creditors *scale their debts in accordance with the Plan which two-thirds of them are willing to accept* and which has been approved by the Court as reasonable and fair, and accept in lieu of payment of money such securities as are specified in the Plan, can be said to be such an arbitrary and unreasonable exercise of the bankruptcy power as to amount to a denial of due process."

The following significant language used was also in the opinion:

> "Under the Act, *he is merely required to accept what two-thirds of those similarly situated are willing to accept*, and what the court has found to be fair and reasonable under the circumstances; and when the situation is viewed realistically, it is readily seen that he is not required to surrender any part of the value either of his securities or of the property available for the payment of his claim. What he in fact gives up is merely the arbitrary power to frustrate the wishes of the great majority of those who have a common interest in the property of the Debtor."

All through the language of this case emphasis is laid upon the consent of two-thirds of the class of creditors to be bound by the plan. This is exactly the contention of the petitioners here.

Campbell v. *Alleghany Corporation* was decided prior to the *Radford* case in which the doctrine is clearly laid down that the owner of a mortgage has substantive rights in specific property which do not depend on the value of the security applicable to the satisfaction of the mortgage indebtedness, and that, therefore, the District Court cannot, by ascertaining the present fair market value of the security, determine that a secured lien is valueless and by such determination wipe out such lien.

Under the authority of the *Radford* case, it is clear that the District Court did not possess the power, even had it found a value in the property of the Debtor exceeding the indebtedness under the first mortgage, to compel the holders of the second and third mortgages to take such excess value in full payment of their liens. Radford con-

tended that he had the right, under the Frazier-Lemke Act, to substitute rights of equivalent value for the rights of the mortgagee on his farm, but this court held that the Louisville Joint Stock Land Bank could refuse to take equivalent values and had the power to insist upon its rights as established by its mortgage.

Despite the pontifical expressions of our adversaries to the contrary, there is nothing holier about first mortgages than second mortgages. Both are inviolable to the extent of the rights they confer. As well as first mortgages may resist reorganization in any form which deprives them of substantive rights in specific property without consent, so may second mortgagees resist reorganization which deprives them of their substantive rights, lower down in the scale of priorities as they may be. As surely as a first mortgagee may foreclose ahead of the second, just that surely may the second mortgagee follow in his footsteps and pick up the property by the exercise of the right of redemption.

CONCLUSION

The *Radford* case so repeatedly referred to in the preceding argument furnishes both the test and the answer to the questions here presented. The opinion replenishes and trims an old beacon which lights the way to the correct conclusion of the issues here presented. Under the language of that opinion the case at bar resolves itself into a simple inquiry:

(1) Does a second mortgage confer upon the second mortgagee substantive rights in specific property of the debtor beyond those rights of a mere general creditor possessing no security?

(2) If a second mortgage does confer rights in specific property, may those rights be divested without the consent of the holders of the indebtedness under Section 77B of the Bankruptcy Act as Amended?

The answer is as simple as the inquiry, and it is:

(1) That a second mortgage does confer substantive rights in specific property.

(2) That Section 77B does not authorize a divestiture of those rights without consent, and

(3) If the Statute does permit such divestiture without consent of any of the holders of the second mortgage indebtedness, then it runs afoul of the Fifth Amendment of the Constitution of the United States under the doctrine of the *Radford* case.

It is earnestly urged that the decree below be reversed and the cause remanded to the District Court, for the Northern District of Illinois, Eastern Division, for such further proceedings as this court may direct.

Respectfully submitted,

THEODORE E. REIN,
ISAAC M. MILLS,
Counsel for Petitioners.

APPENDIX A.

"(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character or otherwise; (3) shall provide for the payment in cash of all costs of administration and other allowances made by the court except that compensation or reimbursement provided for in subdivision (c), clause (9), of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment and the court finds such compensation reasonable; (4) shall provide in respect of each class of stockholders, of which less than a majority shall accept such plan (unless the judge shall determine either that the debtor is insolvent, or that the interest of such class of stockholders will not be affected adversely by the plan), adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with by the plan, either, as provided in the plan, (a) by a sale of the property at not less than a fair upset price, or (b) by appraisal and payment in cash of the value either of their stock, or at the objecting stockholders' election, of the securities allotted to such stockholders under the plan, if any shall be so allotted, or (c) by such methods as will do substantial justice to such stockholders under and consistent with the circumstances

of the particular case; (5) *shall provide in respect of each class of creditors of which less than two thirds in amount shall accept such plan (unless the claims of such class of creditors will not be affected by the plan, or the plan makes provision for the payment of their claims in cash in full), provide adequate protection for the realization by them of the value of their interests, claims, or liens, if the property affected by such interests, claims, or liens is dealt with by the plan,* either as provided in the plan (a) by the transfer or sale of such property subject to such interests, claims, or liens, or by the retention of such property by the debtor subject to such interests, claims, or liens, or (b) by a sale free of such interests, claims, or liens at not less than a fair upset price and the transfer of such interests, claims, or liens to the proceeds of such sale; or (c) *by appraisal and payment either in cash of the value either of such interests, claims or liens or at the objecting creditors' election of the securities allotted to such interest claims or liens under the plan, if any shall be so allotted; or* (d) *by such method as will in the opinion of the judge, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection;* (6) may reject contracts of the debtor which are executory in whole or in part, including unexpired leases except contracts in the public authority; (7) shall, in case any creditor or stockholder or class thereof shall not be affected by the plan, specify the creditor or stockholder or class or classes thereof not affected and contain such provisions with respect thereto as may be appropriate, and in case any controversy shall arise as to whether any creditor or stockholder or class thereof shall or shall not be affected, the issue shall be determined by the judge after hearing upon notice to the parties interested; (8) shall specify what claims, if any, are to be paid in cash in full; (9) shall provide adequate means for the execution of the plan, which

may include the transfer of all or any part of the property of the debtor to another corporation or to other corporations, or the consolidation of the properties of the debtor with those of another corporation, or the merger or consolidation of the debtor into or with another corporation or corporations, or the retention of the property by the debtor, the distribution of assets among creditors or any class thereof, the satisfaction or modification of liens, indentures, or other similar instruments, the curing or waiver of defaults, extension of maturity dates of outstanding securities, the change in interest rates and other terms of such securities, the amendment of the charter of the debtor, and the issuance of securities of either the debtor or any such corporation or corporations, for cash, or in exchange for existing securities, or in satisfaction of claims or rights, or for other appropriate purposes; (10) may deal with all or any part of the property of the debtor and may include any other appropriate provisions not inconsistent with this section. No creditor or stockholder shall, for the purposes of this section be deemed to be affected by any plan of reorganization unless the same shall affect his interests materially and adversely. The term 'securities' shall include evidences of indebtedness, either secured or unsecured, stock, certificates of beneficial interest therein, and certificates of beneficial interest in property. The term 'stockholder' shall include the holders of voting trust certificates. The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interests of whatever character. For all purposes of this section unsecured claims which would

have been entitled to priority over existing mortgages if a receiver in equity of the property of the debtor had been appointed by a Federal court on the day of the approval of the petition or answer under this section, shall be entitled to such priority, and the holders of such claims, and of other claims, if any, of equal rank, shall be treated as a separate class of creditors. In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of re-entry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or re-entry; Provided, That the court shall scrutinize the circumstances of an assignment of future rent claims and the amount of the consideration paid for such assignment in determining the amount of damages allowed assignee hereunder. *In the case of secured claims entitled to the provisions of clause* (5) *of this subdivision* (b), *the value of the security shall be determined in the manner provided in section 57, clause* (h) *of this Act, and if the amount of such value shall be less*

than the amount of the claim, the excess may be classified as an unsecured claim. The provisions of section 60 of this Act shall apply to claims against the debtor in a proceeding under this section. For all purposes of this section any creditor may act in person, by an attorney at law, or by a duly authorized agent or committee: Provided, That the judge shall scrutinize and may disregard any limitations or provisions of any depositary agreements, trust indentures, committee or other authorizations affecting any creditor acting under this section and may enforce an accounting thereunder or restrain the exercise of any power which he finds to be unfair or not consistent with public policy and may limit any claims filed by such committee member or agent, to the actual consideration paid therefor. The running of all periods of time prescribed by any other provisions of this Act, and by all statutes of limitations, shall be suspended during the pendency of a proceeding under this section." (Italics ours.)

APPENDIX B.

(Being Sections 16, 18 and 20 of Chap 77, Smith-Hurd Ill. Rev. Stats. 1931.)

"16. *Certificate.* Sec. 16. When any real estate is sold by virtue of an execution, judgment, or decree of foreclosure of mortgage, or enforcement of mechanics' lien, or vendor's lien, or for the payment of money, it shall be the duty of the sheriff, master in chancery, or other officer, instead of executing a deed for the premises sold, to give to the purchaser a certificate describing the premises purchased by him, showing the amount paid therefor, or if purchased by the person in whose favor the execution or decree is, the amount of his bid, the time when the purchaser will be entitled to a deed, unless the premises shall be redeemed, as provided in this Act."

"18. *Redemption by defendant, etc.* Sec. 18. Any defendant, his heirs, administrators, assigns, or any person interested in the premises, through or under the defendant, may, within twelve months from said sale, redeem the real estate so sold by paying to the purchaser thereof, his executors, administrators or assigns or to the sheriff or master in chancery, or other officer who sold the same, or his successor in office, for the benefit of such purchaser, his executors, administrators or assigns, the sum of money for which the premises were sold or bid off, with interest thereon at the rate of six per centum per annum from the time of such sale, whereupon such sale and certificate shall be null and void."

"20. *Redemption by creditor, etc.* Sec. 20. If such redemption is not made, any decree or judgment creditor, his executors, administrators or assigns may, after the expiration of twelve months and within fifteen months after the sale, redeem the premises in the following manner: Such creditor, his executors, administrators or assigns, may sue out an execution upon his judgment or decree, and place the same in the hands of the sheriff or other proper officer to execute the same, who shall indorse upon the back thereof a levy of the premises desired to be redeemed; and the person desiring to make such redemption shall pay to such officer the amount for which the premises to be redeemed were sold, with interest thereon at the rate of six per centum per annum from the date of the sale, for the use of the purchaser of such premises, his executors, administrators or assigns, whereupon such officer shall make and file in the office of the recorder of the county in which the premises are situated a certificate of such redemption, and shall advertise and offer the premises for sale under said execution as in other cases of sale or execution."

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CHARLES ELMORE CROP
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IN THE

Supreme Court of the United States

October term, A. D. 1936.

No. 271

In the matter of 620 CHURCH STREET BUILDING CORPORATION, a corporation, debtor under section 77B of the bankruptcy act.

620 CHURCH STREET BUILDING CORPORATION, IRENE K. GOODMAN, G. WALLER, M. LONG, A. W. KIBBY, EMIL ROSENTHAL and B. K. GOODMAN,

petitioners,

vs.

WARNER G. BAIRD, trustee of debtor, CHESTER R. DAVIS, MURRAY WOLBACH and JAMES R. McCAHEY, as members of bondholders committee for the holders of first mortgage bonds, LOUIS M. QUITMAN and EDGAR N. GREENEBAUM, as trustees under first mortgage, WILLIAM L. O'CONNELL, as receiver of Central Republic Trust Company, CLARA ABT, LUCILLE ABT, EDWARD SCHOEN and ALICE G. HIRSH,

respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

Brief of the respondents Louis M. Quitman and Edgar N. Greenebaum, first mortgage trustees, in opposition to the petition for certiorari.

HENRY L. KOHN,
ISAAC E. FERGUSON,
both of Chicago, Illinois.

Attorneys for respondents Louis M. Quitman and Edgar N. Greenebaum, as first mortgage trustees.

HOMER LANDAU & CO., CHICAGO, ILLINOIS

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IN THE

SUPREME COURT OF THE UNITED STATES

October term, A. D. 1936.

In the matter of
620 CHURCH STREET BUILDING CORPORATION, a corporation, debtor under section 77B of the bankruptcy act.

620 CHURCH STREET BUILDING CORPORATION, IRENE K. GOODMAN, G. WALLER, M. LONG, A. W. KIBBY, EMIL ROSENTHAL and B. K. GOODMAN,

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WARNER G. BAIRD, trustee of debtor, CHESTER R. DAVIS, MURRAY WOLBACH and JAMES R. McCAHEY, as members of bondholders committee for the holders of first mortgage bonds, LOUIS M. QUITMAN and EDGAR N. GREENEBAUM, as trustees under first mortgage, WILLIAM L. O'CONNELL, as receiver of Central Republic Trust Company, CLARA ABT, LUCILLE ABT, EDWARD SCHOEN and ALICE G. HIRSH,

respondents.

No. 271.

BRIEF OF THE RESPONDENTS LOUIS M. QUITMAN AND EDGAR N. GREENEBAUM, FIRST MORTGAGE TRUSTEES, IN OPPOSITION TO THE PETITION FOR CERTIORARI.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

To the honorable chief justice and associate justices of the Supreme Court of the United States:

The district court found that the fair market value of the debtor's property was $245,025. (R. 15—par. 11.) The debtor's first mortgage indebtedness, at the time of confirmation of the reorganization plan, exceeded $585,832.50.*

* Principal amount $445,500; interest at 6% from January 1, 1931, $140,332.50; total $585,832.50. This does not take account of additional interest at the higher rate of 7% effective after the default of July 1, 1931, also other accrued charges under the first mortgage.

Thus the fair market value of the debtor's property was approximately 40% of the first mortgage indebtedness.

The petitioners, junior creditors and stockholders of the debtor corporation, notwithstanding the clearly valueless character of their interests in the debtor's property, complain that the circuit court of appeals abused its discretion in denying leave to appeal from the order of the district court confirming a plan of reorganization under which their claims were disposed of by appraisal.

After determining the fair value of debtor's property as aforesaid, the court—applying subparagraphs (4) and (5) of subsection (b) of section 77B of the bankruptcy act, as amended June 7, 1934*—made further findings as follows:

> "That the debtor is accordingly insolvent; that the stockholders are not entitled to participate in the plan, and that their acceptance of the plan is not a prerequisite to the confirmation of the plan." (R. 15—par. 11.)
>
> "That the court has appraised and does hereby appraise all claims allowed in class 3 (second mortgage notes) and class 4 (third mortgage note) to be of no value * * * and accordingly no securities, cash, or any

---

* Subsection (b) of section 77B of the bankruptcy act, as amended June 7, 1934, provides as follows (11 USCA, section 207, subsection (b)):

> "A plan of reorganization within the meaning of this section * * * (4) shall provide in respect of each class of stockholders, of which less than a majority shall accept such plan (*unless the judge shall determine either that the debtor is insolvent*, or that the interest of such class of stockholders will not be affected adversely by the plan), adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with by the plan, either, as provided in the plan,
>
> (a) by a sale of the property at not less than a fair upset price, or
>
> (b) by appraisal and payment in cash of the value either of their stock, or at the objecting stockholders' election, of the securities allotted to such stockholders under the plan, if any shall be so allotted, or
>
> (c) by such methods as will do substantial justice to such stockholders under and consistent with the circumstances of the particular case;
>
> (5) shall provide in respect of each class of creditors of which less

other thing of value shall be distributed under the plan in respect of any of the claims allowed in classes 3 and 4, and the acceptance of the plan by the holders of such claims is not a prerequisite to the confirmation of the plan." (R. 15—par. 12.)

"The court further finds that the foregoing method of treatment of the holders of claims of classes 3 and 4 provides adequate protection for the realization by the holders thereof of the value thereof under and consistent with the circumstances of the case, the same being of no value." (R. 15—par. 12.)

Thereupon, pursuant to the consent of the holders of more than two-thirds of first mortgage bonds, the court approved the plan of reorganization. Since the record presented to this court reveals neither the plan of reorganization itself, nor the proceedings of the trial court underlying its approval, the sufficiency of the evidence and regularity of the proceedings are not open to dispute.

There is much argument in the petition for certiorari on the assumption that the value of the debtor's property as found by the court was a "temporary" value, or "forced sale" value. Suffice it to say that what the trial court de-

---

than two thirds in amount shall accept such plan (unless the claims of such class of creditors will not be affected by the plan, or the plan makes provision for the payment of their claims in cash in full), provide adequate protection for the realization by them of the value of their interests, claims or liens, if the property affected by such interests, claims, or liens is dealt with by the plan, either, as provided in the plan,

(a) by the transfer or sale of such property subject to such interests, claims, or liens, or by the retention of such property by the debtor subject to such interests, claims or liens, or

(b) by a sale free of such interests, claims, or liens at not less than a fair upset price and the transfer of such interests, claims, or liens to the proceeds of such sale; or

(c) by appraisal and payment either in cash of the value either of such interests, claims, or liens, or, at the objecting creditors' election, of the securities allotted to such interests, claims, or liens under the plan, if any shall be so allotted; or

(d) by such method as will in the opinion of the judge, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection. * * *"

termined was the "fair market value" of the debtor's property (R. 15) and that there is no basis in the record upon which to characterize the valuation made by the court as a "temporary" or "forced sale" value, or otherwise to question its adequacy.

* * * * * * * * * * *

In opposition to the petition for certiorari, these respondents urge:

(1) No question under the constitution of the United States has been property raised or preserved by petitioners, either in the trial court, the circuit court of appeals, or this court.

(2) The decision of the circuit court of appeals is not in conflict with any decision of this court; nor in conflict with any decision of any other circuit court of appeals.

(3) The petition fails to show any other adequate reason, under rule 38 of this court, why certiorari should be granted.

(1)

No sufficiently definite constitutional question raised.

The objections filed by petitioners to the plan of reorganization are not included in the record before this court. However, in the petition for leave to appeal filed in the circuit court of appeals it is stated: "Petitioners filed objections to said plan which, in substance, were based on the fact that the said plan did not provide adequate protection for the realization by the holders of the second mortgage notes and the holders of the third mortgage note and of the holders of the capital stock of the debtor of the value

of their liens and claims against the debtor's property, and that said plan was unfair and inequitable and contrary to the constitution of the United States of America, in that said plan was repugnant to the fifth amendment to the constitution." (R. 8—par. 10.) Petitioners' assignment of errors, accompanying the petition for leave to appeal, included the following: "That the district court erred in not finding and decreeing that the said plan of reorganization is unfair, inequitable and contrary to the constitution of the United States of America, in that said plan and the order of confirmation thereof are repugnant to the fifth amendment of said constitution." (R. 20—assignment no. 16.)

Obviously, by the aforesaid assignment of error, petitioners raised no question as to the constitutional validity of section 77B of the bankruptcy act in whole or in part. Or, if the objection is that the trial court, in applying the statute, violated rights guaranteed to petitioners by the fifth amendment, nowhere is there any specification of the rights violated or the precise respect in which it is claimed that the court violated such rights.

We submit that no sufficiently definite question of deprivation of rights under the fifth amendment, either by action of congress in enacting section 77B of the bankruptcy act, or by action of the trial court in applying the statute, is presented by the petition for certiorari or the record of this case. (*Seaboard Air Line Ry. Co.* v. *Watson*, 287 U. S. 86 (headnotes 2, 3 and 4).)

(2)

No conflict with decision of this court in Louisville Joint Stock Land Bank v. Radford, 295 U. S. 555.

In the *Radford* case the mortgagor, proceeding under subsection (s) of section 75 of the bankruptcy act, sought to stay recourse of the mortgagee against the mortgaged property for a period of five years, meanwhile to retain ownership and possession of the mortgaged property upon the sole obligation to pay the rental fixed by the court, meanwhile also to have the option to dispose entirely of first mortgage indebtedness of $9,025.09 by repurchase of the property at appraised value of $4,445.

Not to enter upon a discussion of the precise constitutional questions involved in the *Radford* case, certainly there is no analogy between the circumstances of that case and the circumstances of the present case. The interests of the petitioners in the debtor's property were clearly valueless. Petitioners contend nevertheless that, because of their non-consent to the plan of reorganization, procedure by a foreclosure sale, subject to right of redemption, became mandatory. The only question is, then, whether in the exercise of the bankruptcy power the debtor's property could be disposed of in a manner to preclude a sale subject to right of redemption.

If the debtor's property had been sold to satisfy a judgment or lien, under the laws of Illinois the petitioners or some of them might have had the right to redeem. However, bankruptcy disposition of the property is not such a sale. (*American Mining Equipment Company* v. *Illinois Coal Corporation*, 31 F. (2d) 507, 513.) Granted that petitioners' redemption rights were vested property rights under

the laws of Illinois, such property rights were subject to be divested as an incident to the exercise of bankruptcy power. (*Hanover National Bank* v. *Moyses*, 186 U. S. 181; see also *Mottley* v. *Louisville & Nashville Ry. Co.*, 211 U. S. 149.) Under the decisions of this court, it is no longer open to argument that section 77B of the bankruptcy act was not validly passed by congress in the exercise of the bankruptcy power. (*Canadian Southern Railroad Company* v. *Gebhard*, 109 U. S. 527; *Continental Illinois National Bank and Trust Company* v. *Chicago Rock Island & Pacific Ry. Co.*, 294 U. S. 648; *Meyer* v. *Kenmore Granville Hotel Company*, 80 L. ed. (Adv. Op.) 409.)

If the argument were sound that the bankruptcy court cannot divest vested rights, it would be just as applicable to the rights of non-assenting first mortgage bondholders as to the rights of junior mortgage noteholders, therefore sections 77 and 77B of the bankruptcy act would necessarily fall in their entirety.

(3)

No conflict with decisions of other circuit courts of appeal.

Although the courts have vigorously and repeatedly asserted that section 77B may not be invoked by stockholders or junior creditors merely to destroy or cut down the rights of non-assenting *prior lien creditors*, no court has as yet suggested as a converse or corollary that junior creditors and stockholders, no matter how valueless their interests in the debtor's property, must be granted participation in a reorganization under section 77B—at penalty of reversion to the procedure of a foreclosure sale, subject to rights of redemption.

The cases primarily relied on by petitioners insist upon full protection of the interest of first mortgagees, as against demands of junior claimants. (*In re Murel Holding Corporation* (CCA 2), 75 F. (2d) 941; *In re Tennessee Publishing Company* (CCA 6), 81 F. (2d) 463; *Francisco Building Corporation Limited* v. *Battson* (CCA 9), 83 F. (2d) 93.)

The decision of the circuit court of appeals for the seventh circuit in the present case does not in the least conflict with the decision of the same court in the matter of *Georgian Hotel Corporation* (CCA 7), 82 F. (2d) 917. Under the plan of reorganization adopted in that case, with the consent of 94% of the first mortgage bondholders, a portion of the capital stock of the new corporation organized to take over the assets of the debtor corporation was allocated to junior creditors and stockholders. The circuit court of appeals held that approval of this plan was fairly within the judicial discretion of the district court; that under the facts of the particular case the assenting first mortgage bondholders and the trial court might well have regarded the allotment of stock to the holders of junior claims as an equitable offset to the value of their right of redemption, assuming that the case had proceeded by foreclosure in the state court and not by reorganization in the bankruptcy court. There was no holding or intimation that it was obligatory upon the first mortgage bondholders or the trial court, regardless of the present fair market value of the debtor's property, to grant participation in the reorganization to the junior creditors and stockholders.

Conclusion.

There is no inequity to petitioners in the order of the district court, or denial by the circuit court of appeals of leave to appeal. If the estate of the insolvent debtor were ordered liquidated, it is obvious that such liquidation would yield nothing to petitioners upon their junior claims. If the reorganization proceedings were dismissed and the parties relegated to foreclosure proceedings in the state court, foreclosure sale would just as inevitably wipe out the interests of petitioners. The real complaint of the petitioners is that procedure under section 77B of the bankruptcy act makes possible the elimination of "nuisance value" which they might have had if congress, in the exercise of the bankruptcy power, had not afforded procedure other than foreclosure for adjudication and disposition of all claims against the debtor's property.

We respectfully submit that the petition for certiorari should be denied.

HENRY L. KOHN,
ISAAC E. FERGUSON,
both of Chicago, Illinois.

Attorneys for respondents Louis M. Quitman and Edgar N. Greenebaum, as first mortgage trustees.

FILE COPY

SEP 10 1936

CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1936.

No. 271

IN THE MATTER OF 620 CHURCH STREET BUILDING CORPORATION, A CORPORATION, DEBTOR UNDER SECTION 77B OF THE BANKRUPTCY ACT.

620 CHURCH STREET BUILDING CORPORATION, IRENE K. GOODMAN, G. WALLER, M. LONG, A. W. KIBBY, EMIL ROSENTHAL AND B. K. GOODMAN,
Petitioners,

vs.

WARNER G. BAIRD, TRUSTEE OF DEBTOR, CHESTER R. DAVIS, MURRAY WOLBACH AND JAMES R. McCAHEY, AS MEMBERS OF BONDHOLDERS COMMITTEE FOR THE HOLDERS OF FIRST MORTGAGE BONDS, LOUIS M. QUITMAN AND EDGAR N. GREENEBAUM, AS TRUSTEES UNDER FIRST MORTGAGE, WILLIAM L. O'CONNELL, AS RECEIVER OF CENTRAL REPUBLIC TRUST COMPANY, CLARA ABT, LUCILLE ABT, EDWARD SCHOEN AND ALICE G. HIRSH,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

SUGGESTIONS OF CHESTER R. DAVIS, ET AL., IN OPPOSITION TO THE PETITION FOR CERTIORARI.

DON KENNETH JONES,
Attorney for Respondents
Chester R. Davis, et al.

THE GUNTHORP-WARREN PRINTING COMPANY, 310 WEST JACKSON, CHICAGO

IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1936.

No. 271

IN THE MATTER OF 620 CHURCH STREET BUILDING CORPORATION, A CORPORATION, DEBTOR UNDER SECTION 77B OF THE BANKRUPTCY ACT.

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ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

SUGGESTIONS OF CHESTER R. DAVIS, ET AL., IN OPPOSITION TO THE PETITION FOR CERTIORARI.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

The petition for certiorari is improvidently presented. Rule 38, Section 1, provides that the petition "shall be accompanied by a certified transcript of the record in the

case, including the proceedings in the court to which the writ is asked to be directed". The petition at bar was not accompanied by a certified transcript of the record in the case. The only record presented is of certain proceedings had in the Circuit Court of Appeals, the court to which the writ is asked to be directed. The record of the case itself has not been filed.

It is submitted that the petition for certiorari be denied.

DON KENNETH JONES,
Attorney for Respondents
Chester R. Davis, et al.

FILED
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CHARLES ELMORE CRO
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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1936.

No. 271

IN THE MATTER OF 620 CHURCH STREET BUILDING CORPORATION, A CORPORATION, DEBTOR UNDER SECTION 77B OF THE BANKRUPTCY ACT.

620 CHURCH STREET BUILDING CORPORATION, IRENE K. GOODMAN, G. WALLER, M. LONG, A. W. KIBBY, EMIL ROSENTHAL AND B. K. GOODMAN,
Petitioners,

vs.

WARNER G. BAIRD, TRUSTEE OF DEBTOR, CHESTER R. DAVIS, MURRAY WOLBACH AND JAMES B. McCAHEY, AS MEMBERS OF BONDHOLDERS COMMITTEE FOR THE HOLDERS OF FIRST MORTGAGE BONDS, LOUIS M. QUITMAN AND EDGAR N. GREENEBAUM, AS TRUSTEES UNDER FIRST MORTGAGE, WILLIAM L. O'CONNELL, AS RECEIVER OF CENTRAL REPUBLIC TRUST COMPANY, CLARA ABT, LUCILLE ABT, EDWARD SCHOEN AND ALICE G. HIRSH,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

BRIEF OF CHESTER R. DAVIS, MURRAY WOLBACH AND JAMES B. McCAHEY, AS MEMBERS OF BONDHOLDERS COMMITTEE FOR THE HOLDERS OF FIRST MORTGAGE BONDS, AS RESPONDENTS.

GEO. T. BUCKINGHAM,
DON KENNETH JONES,
EDWIN L. HARDING,
Attorneys for Respondents Chester R. Davis, et al.

THE DARTNELL-WARREN PRINTING COMPANY, 310 WEST JACKSON, CHICAGO

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ruptcy proceedings, and proceeded to classify the claims of the Debtor corporation.

4. That the holders of the second and third mortgage notes voluntarily appeared in the District Court proceedings and filed their claims under their mortgage notes, which claims were allowed for the purpose of permitting them representation in the proceedings.

5. That the Debtor and the holders of the second and third mortgage notes actively participated in the proceedings thereafter.

6. That the court heard voluminious evidence on all phases of the situation, and made a finding that the property of the Debtor had a market value of $245,025, and that there was no equity in the estate of the Debtor over and above the $445,500 value of the First Mortgage Bonds, and that the Debtor is insolvent. Notwithstanding the unsupported statement of the argument of petitioner as to what the court found, and upon what evidence the finding was predicated, it is assumed that the finding in the District Court itself, is held conclusive of that question.

7. That the court accordingly approved a plan of reorganization.

It should be stated that the allegations of petitioner's brief as to what that plan is, are entirely unsupported by the record before this court, and are also unsupported by the statement of facts in the petition. It must, therefore, be assumed that the plan was fair, just and equitable, in view of the many and peculiar circumstances of the case which have been omitted from the transcript of the record brought before this court.

8. That the Debtor and the second and third mortgage note holders objected to the plan and actively participated in the proceedings in the District Court relative thereto by negotiation and litigation.

9. That the order of the District Court made an appraisal of *all* the property of the debtor, and also appraised the value of *all* classes of claims; and further as a matter of fact on that appraisal found that the claims of the noteholders of the second and third mortgage, and the claims of the Debtor corporation and its stockholders against the estate, were of *no* value, and that accordingly they were not parties interested in the reorganization, and their specific consent to the plan itself was unnecessary.

Petitioners attack the order of the District Court confirming the plan of reorganization, on two basic grounds:

1. The court made an appraisal of the value of all the property of Debtor, and also of the value of the claims of the junior lienors and of the Debtor and its stockholders. Upon that appraisal, the court found that the value of the claims of those having priority over all mortgage liens, plus the claims of the First Mortgage Bondholders, was greater by far than the value of all the property involved, and that the Debtor was hopelessly insolvent.

Wherefore, the court found that the claims of the junior lienors and of the Debtor and its stockholders were of *no* value, that no distribution of assets should be made among them, and that their consent to the confirmation of the plan was unnecessary.

The petitioners say in criticism of this action, (a) that the second and third mortgage bondholders should have been given something in the distribution of assets, and (b) that their consent was necessary under the law to the confirmation of the plan.

2. The petitioners complain that wholly aside from the right to receive a monetary distribution from the assets, the second and third mortgage lien holders, and the Debtor itself, under Illinois law, had certain rights (a) the right to have the estate of the Debtor sold at a sale; (b) the

right to bid at such sale; and (c) the right of the Debtor to redeem from such sale within twelve months, and the right of the lienors thereafter within three months likewise to redeem.

The petitioners say that these rights were destroyed by the order confirming the plan of reorganization, and that they were not compensated for them, and they, therefore, invoke the protection of the Fifth Amendment.

ARGUMENT.

I.

THE APPROVAL OF THE PLAN OF REORGANIZATION BY THE DISTRICT COURT WITHOUT THE CONSENT OF THE HOLDERS OF TWO-THIRDS IN AMOUNT OF THE SEVERAL JUNIOR INDEBTEDNESS AND WITHOUT COMPENSATION TO THEM IS AUTHORIZED BY SECTION 77B OF THE BANKRUPTCY ACT, AS AMENDED, IF THE COURT FINDS THAT THE CLAIMS OF THE JUNIOR INDEBTEDNESS ARE VALUELESS.

A.

Section 77B, Subdivision (b) (5), provides that adequate protection may be given to a class of creditors of which less than two-thirds consent to a plan of reorganization for the realization by them of the *value* of their interests, claims, or liens,

> "(c) by appraisal and payment either in cash of the *value* either of such interests, claims, or liens, or, at the objecting creditors' election, of the securities allotted to such interests, claims, or liens under the plan, if any, shall be so allotted."

This method of determining the value of the claims of the junior lienors of the Carlson Annex was adopted by the plan of reorganization as is apparent from the action of the District Court set forth in paragraph 12 of its confirmation order. (R. 15.) In paragraph 11 of the confirmation order the District Court, on the basis of evidence and testimony heard by it on the value of the property of the Debtor, found that the Carlson Annex had a fair market value of $245,025 and that there was no equity over and above the $445,500 principal amount of First Mortgage Bonds outstanding against the property of the Debtor, and that the Debtor was accordingly insolvent.

(R. 15.) In paragraph 12 of its confirmation order, the District Court appraised the junior liens to be of no value. (R. 15.) The so-called destruction of the value of these claims is not due to any action of the District Court, but is due to the fact that they have become valueless from an economic standpoint. It is plain that Section 77B (b) (5) (c) does not require that the holders of these claims be paid in cash or securities, that subdivision only requiring that cash or securities be paid to the holder of a claim that has been appraised at some *value*.

Another provision of Section 77B also makes it clear that these claims need not be provided for in the plan of reorganization. Subdivision (b) (10) of Section 77B provides that

> "No creditor or stockholder shall, for the purposes of this section, be deemed to be affected by any plan of reorganization unless the same shall affect his interests *materially and adversely.*"

Subdivision (b) (5) does not require that "adequate protection for the realization" of their claims by a class of creditors be given if their claims will not be affected by the plan. Since the claims based on the junior lien securities in the instant case have been judicially determined to be of no value, the interests of the holders of such claims are not materially and adversely affected by the plan of reorganization, and, therefore, not being affected by the plan, it is not necessary that the holders thereof receive any cash or any new securities or consent to the plan.

B.

The foregoing contentions have adequate support in lower court decisions as well as in reason.

The opinion in *In re Central Funding Corporation*, 75 F. (2nd) 256 (C. C. A. 2nd, 1935), at pages 259, 260, contains the following significant language:

"A 'reorganization' does not necessarily presuppose

the survival of the rights of stockholders or even of junior creditors, when they have become worthless, but may be a readjustment of the rights of the lienors under a new corporate structure. While this has generally been effected through foreclosure sale, such has not always been the method, and Section 77B was evidently inserted in the Bankruptcy Act in order, among other things, to facilitate corporate readjustments without the delay, complexity, and difficulty inherent in the cumbersome methods that were formerly regarded as necessary.

* * * * * *

"A proceeding for a reorganization may be instituted by the debtor or creditors, as was done here, and a creditors' petition may be filed not only where the corporation 'is unable to meet its debts as they mature,' but also where it 'is insolvent'. Section 77B (a) Bankruptcy Act (11 U. S. C. A., Par. 207 (a)). The language of Section 77B (b) indicates that the reorganization may be had though no equity remains in the corporation."

In re William Penn Garage (D. C. Pa., Oct. 7, 1935, C. C. H., Par. 3649), also involved a case where the court found that the securities of the junior lien creditors were valueless, the face amount of the first mortgage far exceeding the value of the debtor's assets. The Court said:

"It is not necessary that provision be made in the plan for stockholders where the debtor is insolvent as is the fact in this case, nor is it necessary that provision be made for junior lien creditors where the lien of such creditors is of no value."

Similar facts were present in the case of *In Re Witherbee Court Corporation* (D. C. S. D. N. Y. Nov. 21, 1935, C. C. H. Par. 3727), and the opinion recites that "The second mortgagee, unsecured creditors and present stockholders are to receive nothing (under the plan of reorganization)." In considering this aspect of the plan the Court used the following language:

"With the claims of the first mortgage bondholders taken at a present figure of $437,000, it is manifest

that there is no substantial value in the second mortgage, the unsecured claims and the stock. It necessarily follows that any plan which contemplates the issuance of stock for those interests is unfair to the first mortgage bondholders, and by the same token the plan which gives the entire ownership, both bonds and stock, to the bondholders is not unfair to any junior interest. * * * The moment it is proved that the value of the debtor's property is less than the first mortgage, no reorganization can be tolerated that gives an interest to junior parties unless they pay fair value in cash or property."

The facts in *Preble Corporation* v. *Wentworth* (C. C. A. 1st, June 3, 1936, C. C. H. Par. 4048), are different than in the foregoing cases in that here the debtor's plan provided that the first mortgage be paid off at a price less than the face value of the mortgage to the benefit of junior creditors. In disapproving the plan and affirming the District Court, the Court used the following language:

"The debtor is insolvent, and the value of the real estate covered by the mortgages is substantially less than the amount of the outstanding first mortgage bonds, and therefore an attempt to appraise the value of these bonds would be discriminating against this class in favor of another class which could not be considered fair and equitable. To take the property from the mortgagee upon an appraisal is an attempt to use a supposed or possible value, over and above the appraisal, for the benefit of other creditors and stockholders. If there is any such surplus value it belongs to the first mortgagee, up to the amount of his debt. If there is none, there is nothing to build on, and there would seem to be no object in having an appraisal, in the absence of a disclosure of a method of raising the money, unless junior interests are prepared to advance the money on a chance of increased value in the future, and there is no information before the court to that effect."

Subdivision (e) of Section 77, relating to the reorganization of railroads, was amended on August 27, 1935, so as expressly to permit the consummation of a plan of

reorganization of a railroad without the consent of the holders of junior securities and without compensation to them if the Interstate Commerce Commission shall have found, and the Judge shall have affirmed the finding, that the claims of such junior securities are valueless, such provisions of Subdivision (e) being as follows:

> "Provided, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, *or that at time of the finding the equity of such class of stockholders has no value,* or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: Provided, further, That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, *or that at the time of the finding the interests of such class of creditors have no value,* or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests."

This Section was construed by District Judge Hincks *In re New York, New Haven and Hartford Railroad Co.,* decided September 15, 1936, U. S. D. C. Conn., reported at paragraph 4172 of Commerce Clearing House Bankruptcy Law Service, in which the Court said in part as follows:

> "For, as observed earlier in this memorandum, under the Act only a plan which is free from confiscatory features may be confirmed. To be sure, under the Act the court may approve a plan 'modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured,' etc. But since only an equitable plan may be approved, the plan must provide that every creditor in the order of his priority shall

receive under the plan rights which in equity are the fair equivalent of such of his rights as have been subjected to equitable modification, at least in so far as the assets of the debtor's estate permit. Any creditor found to be only partially secured is entitled to the equitable equivalent of such security as he has, with a right to share in equality with common creditors for the excess of his claim as allowed above the value of his security as ascertained by equitable considerations. And the plan must recognize the prior right of common creditors with respect to such assets as remain after equitable treatment has been accorded to secured creditors. *Kansas City Ry.* v. *Central Union Trust Co.*, 271 U. S. 445. Such is the intent of the Act; surely the substance of a plan of reorganization conforming to that intent cannot conflict with the Fifth Amendment.

"Out of the numerous reorganization cases in the courts of equity, I have been unable to find one that is inconsistent with the principles expressed above. In most of these cases the power of the court, either with or without judicial sale, to enforce the interchange of securities equivalent in equity, has been assumed. • • • ."

C.

The cases cited by the petitioners are absolutely consistent with the foregoing principles. Four of these cases involve situations where a junior interest is attempting to have the claim of the senior interest reduced by appraisal to the benefit of junior interests.

In *Tennessee Publishing Co.* v. *American National Bank*, 81 Fed. (2d) 463 (C. C. A. 6th) the Court refused to allow the reduction of senior lien claims to the benefit of junior interests.

In *In re Murel Holding Corporation*, 75 Fed. (2nd) 941 (C. C. A. 2nd), an order staying a foreclosure proceeding was reversed when it appeared that the only plan proposed was that of the debtor proposing a ten-year extension of the first mortgage and a release of amortization payments.

The court objected to such a plan and pointed out that 77B (b) (5) requires that " 'adequate protection' (of the claims of a dissenting class) must be completely compensatory."

In *Francisco Building Corporation, Ltd.*, v. *Battson*, 83 Fed. (2nd) 93 (C. C. A. 9th), we again find the court refusing to allow the reduction of senior lien claims to the benefit of junior interests. To the same effect is *Security-First National Bank* v. *Rindge Land & Nav. Co.*, C. C. A. 9th, decided August 17, 1936, and reported at Par. 4144 C. C. H. Bankruptcy Law Service.

Also in *In Re Hotel Charles*, 12 Fed. Supp. 734, 736, (affirmed sub nom. *City of Springfield* v. *Hotel Charles Co.*, C. C. A. 1st, 1936, Par. 4054 C. C. H. Bankruptcy Law Service), the Court answered the contention of a municipality, holding a tax lien of $100,000 against a property assessed at $721,100, that it was being deprived of the full value of its security by the order enjoining its foreclosure suit by pointing out that:

> "If any creditor claims a lien upon the property affected by the plan of reorganization and he does not belong to a class of duly assenting creditors, the plan cannot be confirmed unless it provides adequate protection for the realization by the creditor of the *value* of his interest or lien in or upon the property." (Italics ours.)

Likewise, *Louisville Joint Stock Land Bank* vs. *Radford*, 295 U. S. 555, is in line with the foregoing cases inasmuch as it declared an act unconstitutional which deprived a secured creditor of substantive rights to control his security to the benefit of a junior interest, the debtor. It is believed that the Sixth Circuit, in its decision in the Tennessee Publishing Company case, properly held that Section 77B (b) (5) (c) was unconstitutional if, as that court believed, it authorized a substantial reduction in the rights of a first lienor without consent of the holders of two-thirds thereof. On the other hand, it is well settled that a statute susceptible of

two constructions, one constitutional and one unconstitutional, will not be construed to be invalid.

This doctrine is applicable to this statute, and it is believed that the Sixth Circuit was in error in ignoring the distinction between the two situations which may arise under subdivision (b) (5) of Section 77B. In the first class of cases, the shareholders or the junior creditors, without any equity in the debtor's assets, are seeking to have a plan of reorganization confirmed without the consent of the senior lienors. The facts of the Tennessee Publishing case fall within this class, as do the facts of the Radford case, which is the basis for the Tennessee Publishing Co. decision. However, there is a second situation wherein the senior lienor has proposed, or at least has accepted, a plan to which the consent of two-thirds of certain subordinate classes of creditors cannot be obtained. In this situation, to permit stockholders to override the interest of creditors would involve precisely the sort of unwarranted taking of property which was condemned in the *Radford* case. To permit junior creditors to prevail over senior lienors would be only slightly less obnoxious. See "Reorganization Without Consent of Creditors," 34 Mich. L. Rev. 1201 (1936).

In *Louisville Trust Co.* v. *Louisville N. A. & C. R. Co.*, 174 U. S. 674 and in the line of cases following the Boyd case, this court established the principle that the prior rights of creditors must be respected. In the Louisville Trust Co. case, *supra*, this court stated (page 684):

> "* * the stockholder's interest in the property is subordinate to the rights of creditors; first of secured and then of unsecured creditors. And any arrangement of the parties by which the subordinate rights and interests of the stockholders are attempted to be secured at the expense of the prior rights of either class of creditors comes within judicial denunciation."

In *Kansas City Terminal R. Co.* v. *Central Union Trust Co.*, 271 U. S. 445, this court stated:

> "Unsecured creditors of insolvent corporations are

> entitled to the benefit of *the values which remain after lienholders are satisfied* * *.
>
> * * to the extent of their debts creditors are entitled to priority over stockholders against all the property of an insolvent corporation * *. No offer is fair which does not recognize the prior rights of creditors * *. Whenever assessments are demanded, they must be adjusted *with the purpose of according to the creditor his full right of priority against the corporate assets,* so far as possible in the existing circumstances."

The common principle enunciated in these cases is that the Bankruptcy Act does not authorize a court to compel senior lienors with an equity in a debtor's assets to share the security with junior lienors without an equity in the debtor's assets. To confirm a plan of reorganization providing for the delivery of the property involved therein to or upon the order of the senior lienors where there is no equity over and above the amount of the senior lien does not take away any interest of a junior lienor because the value of the interest of the junior lienor (if it ever existed) has vanished by reason of the shrinkage of the value of the property below the amount of the senior lien.

In the instant case the value of the Carlson Annex has shrunk so far below the principal amount of the First Mortgage Bonds that the First Mortgage Bondholders, recognizing the realities of the situation, have accepted a plan of reorganization which provides for the transfer of the Carlson Annex for a consideration amounting to 55 per cent of the principal amount of the First Mortgage Bonds, wholly disregarding accumulations of interest thereon since January 1, 1931.

It is therefore respectfully submitted that the junior creditors of the Carlson Annex cannot attack the action of the District Court in construing Section 77B as not requiring the creation of an artificial value in their claims inasmuch as the appraisal of the Carlson Annex determined

that it was of substantially less value than the claim of the senior lienor.

D.

Furthermore, this court must decide this case on the assumption that the District Court's appraisal was reasonable, since neither the method of valuation nor the supporting testimony are in the record submitted to this Court.

To summarize the effect of the foregoing Argument, it is our belief that it shows that the District Court properly construed and applied Section 77B (b) (5) (c), that it properly valued the claims of the petitioners and that subdivision (b) (5) (c) of Section 77B is constitutional, unless the deprivation of the right of junior interests, who have no real equity in the Debtor's assets, to have a public judicial sale, to bid at the sale, and to have the right to redeem from the sale, is so substantial a deprivation, even though authorized by Section 77B, of the Bankruptcy Act, as to be forbidden by the Fifth Amendment.

The remainder of our brief will consider the latter question.

II.

THE RIGHTS OF JUNIOR LIENHOLDERS ACQUIRED PRIOR TO THE ENACTMENT OF SECTION 77B, INCLUDING THE RIGHT TO INSIST UPON A PUBLIC, JUDICIAL SALE, THE RIGHT TO BID AT SUCH SALE AND THE RIGHT TO REDEEM WITHIN FIFTEEN MONTHS AFTER SALE (EVEN IF SUCH RIGHTS EXIST) ARE RIGHTS WHICH CAN BE DISREGARDED IN CONSUMMATING A PLAN OF REORGANIZATION UNDER SECTION 77B WITHOUT THE CONSENT OF SUCH JUNIOR LIENHOLDERS IN A CASE WHERE THEIR CLAIMS HAVE NO VALUE, PARTICULARLY WHERE THE CLAIM OF THE SENIOR LIENHOLDER GREATLY EXCEEDS THE VALUE OF THE SECURITY, AS IN THE INSTANT CASE.

A.

Section 77B (a) provides in part:

> "* * * the court * * * may exercise all the powers, not inconsistent with this section, which a federal court would have had it appointed a receiver in equity of the property of the debtor by reason of its inability to pay its debts as they mature."

The pertinent part of subdivision (o) of Section 77B reads:

> "In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court * * * shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered * * *."

It is therefore apparent that any powers which the bankruptcy or equity courts could exercise can be exercised by the reorganization court if those powers are not inconsistent with 77B. The following consideration of bankruptcy and equity cases is thought to indicate that the power which the Carlson Annex requires the court to assume under authority of Section 77B (b) (5) (c) is a power which could

be exercised by either bankruptcy or equity courts before the enactment of 77B.

1. It is established that the Bankruptcy Court has the power to sell free and clear of liens. *Van Huffel* v. *Harkelrode,* 284 U. S. 225 (1931). However, the *Radford* case is quoted by the petitioners (See page 29 of the petition for certiorari), to the effect that bankruptcy sales, free and clear of liens, cannot be made "to the prejudice of the lienor in the interest of either the debtor or other creditors." In answer to this, it may be said that the sale in the Carlson Annex case is for the benefit of the first lienor and is not prejudicial to junior liens, since the property is worth only 55 per cent of the first mortgage indebtedness. It is true that sales in bankruptcy have not often been approved if it appears that the amount of the encumbrance exceeds the value of the property. However, this is because prior to the enactment of the reorganization sections of the Bankruptcy Act unsecured creditors were the particular concern of the Bankruptcy Court, and because the question of who should pay certain costs of bankruptcy administration is sometimes embarrassing if there is no surplus over the claims of lienholders. See *Kimmel* v. *Crocker,* 72 F. (2nd) 599 (C. C. A. 10th, 1934); *In Re Cogley,* 107 Fed. 73, (D. C. Iowa, 1901), and *Bonner* v. *Cannon,* 60 F. (2nd) 228 (C. C. A. 10th, 1932). These cases are inapplicable to a reorganization proceeding under Section 77B whose primary concern is the creation of a financially sound business concern rather than the unsecured creditor.

2. Petitioners object to a private sale based on an appraised valuation which is not large enough to provide any proceeds in which junior creditors may share.

However, it is established:

(a) That a bankruptcy court has the power to make private sales. *In re Edes,* 135 Fed. 595 (D. C. Me., 1905); *In re Nevada-Utah Mines & Smelter Corpora-*

tion, 202 Fed. 126 (C. C. A. 2nd, 1913); General Order 18 (2); and that

(b) The power to sell at appraised valuations has been assumed by the equity court in receiverships.

In *Daniel* v. *Layton,* 75 F. (2nd) 135 (C. C. A. 7th, 1935), the court said that "in determining fairness the court may, in cases like the instant one, accept appraisal values instead of resorting to liquidation through sales, etc." The court in the last mentioned case cited *Coriell* v. *Morris White, Inc.,* 54 F. (2nd) 255 (C. C. A. 2nd, 1931), but went on to say, "Even in the absence of precedent, we think such a plan must meet approval. The contentions of one creditor must be considered in the light of their effect on other creditors." The Supreme Court reversed the lower court's decision in the Coriell case in an opinion reported in 289 U. S. 426, but did not condemn a sale at an appraised valuation *per se,* only objecting to the procedure adopted by which the valuation was to be obtained.

Section 77B (c) (2) provides, in part, that:

"every such trustee * * * shall * * * exercise, * * *, all the powers of a trustee appointed pursuant to section 44 of this Act, and if authorized by the judge, the same powers as those exercised by a receiver in equity * * *."

In *In Re Finco Dye and Print Works, Inc.* (D. C. N. Y., June 24, 1936, C. C. H. Bankruptcy Law Service, Par. 4128), a trustee in a 77B proceeding was empowered to make a private sale of the Debtor's real estate where it appeared that the price was adequate. The court said:

"The Court has been unable to find any case wherein comment upon this precise point was made. The case of *In re Allied Owners Corporation,* 4 F. Supp. 684 (1935), justifies the conclusion that in the absence of opposing authority or specific prohibition in the statute, the powers exercised by a receiver in equity and conferred upon trustees under Section 77B (c) (2) are sufficient to permit this court to grant the instant application."

Under Section 77B (a) the Bankruptcy Court, itself, would have the same power.

Clause 5 of Section 77B (b) provides that a class of creditors may have their claims adequately protected "by a sale free of such interests, claims, or liens, at not less than a fair upset price." If there were a sale free and clear of liens in the instant case, the first mortgage bondholders would undoubtedly receive all the net proceeds since their claims far exceed the value of the Debtor's assets.

A further argument which lessens the force of a constitutional attack on the power of the court to sell at an appraisal figure is the long custom of equity courts to fix upset prices. It is well known that the bid seldom materially exceeds the upset price, and there is no reason why appraisal figures would not average as high as upset prices, since too low an appraisal figure would indicate an abuse of discretion just as would too low an upset price. The only difference between the two bases for selling corporate properties is that the upset price is accompanied by a public sale. It is difficult to understand why the absence of the mere formality of a public sale invalidates a sale at an appraised valuation, particularly when it would always be possible for the first mortgage bondholders committee to outbid the junior lienors, through the use of the deposited bonds in making payment of the bid price. As this court stated i *Northern Pacific Railway* v. *Boyd*, 228 U. S. 482, as against creditors, such a sale is "a mere form." Practically it has proven impossible to sell large properties of the character here involved for cash because the large amount of cash required by the upset price renders the bondholders committee, which ordinarily controls a large amount of the outstanding securities, practically the only bidder. (See *First National Bank* v. *Flershem*, 290 U. S. 504 (1934) and *Kansas City Terminal R. Co.* v. *Central Union Trust Co.*, 271 U. S. 445, 455).

Furthermore, the upset price is not often large enough to provide cash for any other dissenters than those found in the ranks of the first mortgage bondholders. Generally all junior interests have had to take either nothing or a minor participation, often based on a cash assessment. Attacks on the upset price reorganization have been confined chiefly to attacks on the upset price by dissenting first mortgage bondholders and to attacks alleging violation of the "fixed principle" of the *Boyd* case (*Northern Pacific R. Co.* v. *Boyd*, 228 U. S. 482). It would seem that "appraisal" reorganizations under Section 77B should only be subject to similar attacks.

Consequently it is believed that the transfer of the Carlson Annex Building to the 636 Church Street Building Corporation at an appraised valuation should be upheld, since this Court cannot go into the question of the adequacy of the valuation on the record submitted to it and should therefore assume that the valuation was proper.

3. Petitioners also contend that the confirmed plan of reorganization is unconstitutional in that it deprives them of their right, or supposed right, to have the value of their respective equities determined by a public judicial sale.

On September 15, 1936, District Judge Hincks, in *In Re New York, New Haven & Hartford R. R. Co., supra*, considered in detail this question, and we are taking the liberty of setting forth excerpts from his opinion, as related to this subject, as Appendix "A".

4. Another constitutional objection to the plan confirmed by the District Court is that junior interests have their equity of redemption cut off. Nevertheless, under the decisions, the rule seems to be that state redemption statutes do not apply to sales by a receiver or trustee holding property in equity receiverships.

In *Blair* v. *Illinois Steel Co.*, 159 Ill. 350, 363, 42 N. E. 895

(1896), there was a proceeding to administer a debtor's assets and dissolve the corporation under the Illinois State dissolution statute. The decree for a sale free of the equity of redemption was held to be proper, because the sale did not come within the state redemption statute which applied to sales "by virtue of an execution, judgment or decree of foreclosure of mortgage or enforcement of mechanics' or vendors' liens or for the payment of money". The property of the Carlson Annex is located in Illinois, and the power of the Federal Court proceeding under Section 77B of the bankruptcy law would seem to be no less than that of an Illinois state court proceeding under a state dissolution statute.

Likewise, in *American Mine Equipment Co.* v. *Illinois Coal Corporation*, 31 F. (2nd) 507 (C. C. A. 7th, 1929), and *Beet Growers' Sugar Co.* v. *Columbia Trust Co.*, 3 F. (2nd) 755 (C. C. A. 9th, 1925), equity receivers were authorized to make sales free of the right of redemption, the court interpreting the state redemption statute there involved as not applying to sales by a trustee or receiver in a proceeding instituted for the benefit of creditors.

The remaining question is whether the statute also fails to cover sales in a 77B proceeding. If the Illinois statute applies to such sales, it is because a sale in a 77B proceeding is a sale on an execution, judgment, decree of foreclosure of mortgage, or a sale for the payment of money. Since the statute is in derogation of the common law, it is to be strictly construed. Whether or not a sale pursuant to a 77B proceeding falls within any of those statutory categories depends upon a determination of the basic purpose of the sale. Its basic purpose does not seem to be the satisfaction of a judgment, execution, foreclosure decree, or to obtain the payment of money. Rather, its basic purpose is to provide a means by which a corporate property may be promptly reorganized so that it may continue to do

business for the benefit of employees, the public, and any of its creditors who may have an equity in its assets. It is therefore submitted that a sale pursuant to a 77B proceeding is not subject to the redemption statute of the State of Illinois.

B.

In conclusion, it is to be noted that the right of redemption is not such an interest in land that it can be administered under Section 75 (s) of the Bankruptcy Act. (*In re Borgelt*, 79 F. (2nd) 929 (1935)), and it seems improbable that a junior lienor, whose security is of much less value than the claim of the senior lienor, has such a substantial property interest in the right to a public, judicial sale, the right to bid at the sale, and the right to redeem, that the loss of this right, under the sanction of the bankruptcy power, amounts to a violation of the Fifth Amendment.

The petitioners attempt to support the right of redemption as a substantial property interest by citing cases where the right has been recognized by state and federal courts, but none of these cases involves a situation where the state statute is in conflict with a power asserted by a federal bankruptcy court except the *Radford* case.

We will not repeat our argument that the *Radford* case is not in conflict with the power assumed by the District Court.

The quotation from *In re Georgian Hotel Corporation*, 82 F. (2d) 917 (Petitioners' Brief, page 34), to the effect that the right to redeem might have been of value to the subordinate creditors of the debtor, was preceded by the following statement of the Court:

> "As to allotment of 30 per cent of the stock to the subordinate creditors, we believe that this was fairly within the judicial discretion of the District Court."

Plainly, the opinion of the court did not recognize that the right of subordinate creditors to redeem should be observed, but only that it might be. Because a court *may* create an artificial equity for junior lienholders does not mean that if it does not create such an equity it is proceeding in an unconstitutional manner.

The act of confirming a plan of reorganization is certainly no more drastic than the act of approving a discharge, and therefore the following quotation from *Hanover National Bank* v. *Moyses*, 186 U. S. 181 (1902), seems pertinent:

> "Congress may prescribe any regulations concerning discharge in bankruptcy that are not so grossly unreasonable as to be incompatible with fundamental law, and we cannot find anything in this act on that subject which would justify us in overthrowing its action."

C.

It is axiomatic that the courts of the United States in working out plans for reorganization under 77B, will protect and preserve any right which any litigant possesses under the laws of the state where the proceedings occur.

At the threshold of this controversy, therefore, arises the instant question—what are the rights of these second and third lien noteholders under Illinois law, and what rights of redemption have they which were necessary to be protected under the reorganization plan?

The right that is alleged by the petition is the right of redemption under the Illinois statutes.

Chapter 77, Section 16 of the Illinois Statutes—Smith-Hurd Revised Statutes, 1935, provides:

> "*When any real estate is sold by virtue of an execution, judgment, or decree of foreclosure of mortgage, or enforcement of mechanic's lien, or vendor's lien, or for the payment of money,* it shall be the duty of the sheriff, master in chancery or other officer, except as

otherwise in this act provided, instead of executing a deed for the premises sold, to give to the purchaser a certificate describing the premises purchased by him, showing the amount paid therefor, or if purchased by the person in whose favor the execution is taken or the decree is entered, the amount of his bid, the time when the purchaser will be entitled to a deed, unless the premises shall be redeemed, as provided in this Act."

It is provided by Section 18:

"*Any defendant*, his heirs, executors, administrators, assigns, or any person interested in the premises, through or under the defendant may * * * within twelve months from said sale, redeem the real estate so sold * * *."

It is also provided by Section 20:

"If such redemption is not made, *any decree or judgment creditor*, his heirs, executors, administrators or assigns may, after the expiration of twelve months and within fifteen months after the sale, and when any sale is had under any order or decree of foreclosure upon a mortgage or trust deed * * * redeem the premises * * *."

Complete copy of said Sections 16, 18 and 20 is attached as Appendix B.

The assignment of error does not claim that the Debtor itself, or the stockholders of the Debtor, had any right of redemption at the time of the entry of the order by the District Court approving the plan of reorganization.

The only other persons under Illinois law who have any right of redemption are "*any defendant*" and a "*decree or judgment creditor*".

It is not alleged in the petition that the second and third mortgage noteholders were "*decree or judgment creditors*". In fact the contrary appears—they were mere lienors, who had not reduced their claims to "decree or judgment" against the Debtor and, under Illinois law, are not persons who now possess any right of redemption.

Furthermore, it appears that originally the Trustee under the Trust Deed securing the first mortgage bonds,

commenced in an Illinois court, a suit for foreclosure, to which the Debtor was necessarily a party defendant. While that suit was pending, *the Debtor itself, by its voluntary petition brought the whole controversy into the District Court of the United States under a 77B petition.*

By that act, it subjected itself and all those who claimed under it, *and all its property,* including its right of redemption, if any, to the District Court, which under bankruptcy law has all the powers of a court of equity, and asked that court to ascertain who were its creditors, to ascertain their respective claims and rights, and to devote all its property, by way of reorganization, to a satisfaction of their respective rights.

Subsequently, *and also of their own volition,* the holders of the second and third mortgage notes, who are the petitioners, and whose rights of redemption are alleged to have been violated, voluntarily appeared in the 77B proceedings, and subjected themselves *and their claims* to the jurisdiction of the bankruptcy court, and thereafter took an active and militant part in the proceedings thereof.

They besought the court to formulate some plan of reorganization, actively assisted in that formulation, and continued active until after the court had approved a plan. Under these circumstances, it is contended by these respondents: *first,* that the second and third mortgage noteholders, concerning whose rights the errors are alleged, were never and are not now the owners of any right of redemption under the Illinois Statutes; and *second,* that if they ever possessed any right of redemption, they waived the same and placed it at the Court's disposal, by their voluntary appearance and participation in the proceedings of the District Court in the Bankruptcy proceedings.

It is likewise contended that the Debtor itself and its stockholders never possessed any right of redemption under Illinois law as to anything *except a sale under a foreclosure,* and that that right was waived by their voluntarily

abandoning the Illinois state tribunal, and voluntarily subjecting all and singular any and all rights they had to the disposition of the District Court of the United States in the Bankruptcy proceedings.

These principles have been firmly imbedded in the law beginning with the case of *Blair* v. *Illinois Steel Company*, 159 Illinois 350, 42 N. E. 895, which is the law in Illinois and has never been overruled, modified or even criticized.

Furthermore, that principle, as stated in *Blair* v. *Illinois Steel Company*, was specifically approved and ratified in an extended discussion by the United States Circuit Court of Appeals, Seventh Circuit, in the case of *American Mine Equipment Company* v. *Illinois Coal Corporation*, 31 Fed. (2d) 507, 510 *et seq.*

These two cases dealt with the right of redemption under the Illinois law, and held that when one, who has a right of redemption in the Illinois court under a foreclosure proceeding, *voluntarily consents that the subject matter be taken by a court of equity in a general receivership suit, or invokes that jurisdiction by his own specific acts, he thereby waives the right of redemption, or what is the same thing, subjects it to the jurisdiction of the equity court, and that court in its plenary power has the right to dispose of the real estate free and clear of the right of redemption.*

The Blair case was again reviewed, and after extended discussion, fully ratified and approved, as to the principle here announced, in *Beet Growers Sugar Company* v. *Columbia Trust Company*, 3 Fed. (2d) 755-57.

It is axiomatic that the United States District Court in a Bankruptcy proceeding under 77B possesses all the power which a court of equity has under a general creditor's bill.

If, therefore, the holders of the second and third mortgage notes were in fact *"decree or judgment creditors"*

(which they are not) and if they had ever possessed a right to redeem as such or as *any defendant*, that right was waived by them when they abandoned the Illinois state jurisdiction in which their claims were originally involved, and invoked the powers of the bankruptcy court, submitted themselves to its jurisdiction, and actively participated in the suit there pending.

It is also obvious that when these second and third mortgage noteholders, who were mere lienors and not "decree or judgment creditors", abandoned whatever right to redemption they may have possessed in the Illinois court, they necessarily also abandoned and waived the right to a sale and the right to bid at it.

The Statute Law of Illinois does not specifically require a sale, in a general equity suit. It is contended by petitioner that the Illinois Statute inferentially recognizes that a sale will take place in a foreclosure suit. Even if that position were sound, it is fully answered by the fact that this proceeding, into which petitioners *voluntarily* came, is *not* a foreclosure suit, but is the equivalent of a general equity suit to wind up corporate affairs.

Under the Illinois Statute no right to *redeem* exists in anyone, unless there is a sale, under foreclosure or judgment. Here there was none. If there *is* such sale, then *any defendant* has a primary and a creditor, *who has obtained a judgment or decree,* has a secondary, or alternative right to redeem. These noteholders were mere lienholders, not judgment creditors. No Illinois statute gives a junior lienor, *as such,* the right to redeem from any sale, in any court.

It may be here assumed that the right to redeem from a foreclosure sale is, under Illinois law, a property right in anyone who possesses the right to redeem. It is equally obvious that if there is no right to redeem, because (1) it never existed in these second and third mortgage noteholders, and (2) that if it ever existed, it was waived by

them, then the right to a sale and the right to bid necessarily fall with the right of redemption.

The right itself exists only as to a sale under foreclosure, etc., and if there is no such sale, then obviously none of these rights have any existence.

Furthermore, there is nothing in the fragmentary record before this court, nor in the order of the District Court, confirming the plan of reorganization which indicate whether the plan contemplates a sale, or whether it does not. It is alleged by the brief of petitioner that no sale was provided for, but there is nothing before this court other than the bare assertion of petitioner's brief on which to predicate that asserted fact.

The contention of the petitioner then amounts to this—that although the debtor and the junior lienors, affirmatively brought *all* the property, and *all* their claims against it, into the bankruptcy court, which was clothed with all the powers of an equity court, and asked that court under 77B to marshal and apportion the property and the debts; and although it developed from the evidence, and the court made a specific finding that all the property thus submitted to it was of a value of only 55 per cent of the First Mortgage claims, *yet* no plan can be approved by the court until the junior lienors and the debtor and its stockholders, who had no pecuniary interest in the subject matter, and who had waived any possible right they might have had to redeem, must first approve the plan. Such a contention leads to an absurd conclusion. In that situation no plan could ever be approved without junior interests, whose interests were not materially or adversely affected, specifically voted to approve the plan.

Indeed, under the situation here presented inadequate as that presentation is, the court of equity would have been derelict in its duty and would have prejudicially affected

the rights of the first mortgage bondholders, if it had awarded any portion of the insolvent estate to these junior claims.

All of which is respectfully submitted.

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APPENDIX A.

Excerpts from opinion of Judge Hincks In re New York, New Haven and Hartford R. R. Co. (U. S. D. C. Conn. Decided September 15, 1936), reported at Par. 4172, Commerce Clearing House, Bankruptcy Law Service.

"We are left then only with the question whether the challenged provision is unconstitutional in that it deprives creditors of a right, or supposed right, to have the value of their respective equities determined by a public judicial sale. In answering this question, it will be helpful to consider whether a court of general equity jurisdiction has power in a proper case by decree, without a judicial sale, to approve and enforce a plan of corporate reorganization.

"This important question, the Supreme Court seems never to have decided. See *First National Bank* v. *Flershem,* 290 U. S. 504, note 7 beginning on page 515. But in *Phipps, et al.* v. *Chicago, R. I. & P. Railway Co.,* 284 Fed. 945, in a carefully reasoned decision it was held that even without the aid of an enabling statute the court of equity had plenary power without a judicial sale to approve and enforce a plan of reorganization. To be sure, the value of that decision as a precedent is somewhat weakened by the fact that after certiorari had been granted (261 U. S. 611), it was thereafter dismissed by stipulation between the parties. (262 U. S. 762.) However, the doctrine has been persistently reaffirmed in the Eighth Circuit. *Royal Union Life Ins. Co.* v. *Gross,* 76 Fed. (2nd) 219; *Warner Brothers Pictures, Inc.* v. *Lawton-Byrne-Bruner Ins. A. Co.,* 79 Fed. (2nd) 804. In effect, I think, the case of *Coriell* v. *Morris White, Inc.,* 54 Fed. (2nd) 255, in the Second Circuit lends support to that conclusion. In that case the District Court had approved a plan of reorganization which was effective to put the assets of the corporate defendant into the new corporation wholly owned by the defendant's stockholders, although under the plan unsecured creditors had been offered in payment of their claims only 80 per cent of the par value thereof in preferred stock and 20 per

cent in deferred notes. Under the plan, the transfer was accomplished on order of court without public sale or competitive bids. Under these circumstances it was held that an objecting creditor could not be compelled to accept what was offered under the plan 'without being afforded the alternative of receiving his proportionate share of the proceeds of the conventional sale of the property in cash.' Thus plainly the court viewed a judicial sale in reorganization proceedings as a mere convention, and emphasized that view by holding that the defect in the plan just noted might be cured and the objecting creditors fully protected by an appraisal of their claims by a master who should ascertain 'the value of the assets as if sold at a public sale,' and on that basis ascertain the 'sum of money that would have been realized had a sale taken place' and award to objecting creditors 'their aliquot share of the assets' in cash on that basis. Thus the holding, essentially as in the cases cited from the Eighth Circuit, was to the effect that a judicial sale may be dispensed with, provided some other arrangement is substituted which guarantees objecting creditors a judicial hearing on the fairness of their treatment under the plan.

"This decision, to be sure, was reversed in *National Surety Co.* v. *Coriell*, 289 U. S. 426. But the Supreme Court, in reversing the decision, was careful to base its decision not at all upon the proposition that a judicial sale is a prerequisite to a valid reorganization. As to this, it said only: 'the non-assenting creditors were entitled to have the plan and their objections considered in an orderly way, and to a decree based on adequate data.' It was pointed out that the District Court had undertaken 'to pass upon the wisdom and fairness of the plan of reorganization and the rights of non-assenting creditors.' It was ordered that the decree of the District Court be vacated, not because the court was without equitable power to pass upon such questions, but because 'for the proper disposition of these questions, definite, detailed, and authentic information was essential. Such information was wholly lacking' in the record of that case. Accurate and complete data, it was said, 'might have influenced the court in deciding whether the plan *should be approved or should be approved only upon a public sale.* The

failure to require relevant data before deciding whether the plan should be approved was not cured by the declaration of the Circuit Court of Appeals that the dissenting creditors were entitled to an aliquot share of what, a year later, it was estimated the property would have brought at a public sale, and authorizing them to recover that amount, if assets to satisfy their claims were then available.' The ruling thus proceeds not on the proposition that a judicial sale is a prerequisite to reorganization in equity, but rather upon the theory that an appraisal made over a year after the plan was approved subjected objecting creditors to the hazard of loss resulting from operations in the meantime. See *First National Bank* v. *Flershem, supra.* 290 U. S., note 8, on page 516.

"And the Flershem case, just referred to, contains a similar implication. There, too, the District Court was reversed and the case remanded not upon a mandate again to offer the corporate assets upon a judicial sale at a corrected upset price, but rather 'for the purpose of ascertaining the sum' which the appellant creditor 'would have received if the property had been sold at a proper price.' Clearly the decision contemplated that the ascertainment would be accomplished through the process of a judicial hearing, but that the required ascertainment when once accomplished had to be translated into a revised upset price and followed by the elaborate and costly procedure of a judicial sale, is not intimated.

"To be sure, in all the cases discussed above the rights of unsecured creditors only were directly in issue. And the contention is here made, largely in reliance upon the doctrine of *Louisville Bank* v. *Radford,* 295 U. S. 555, that the right of a secured creditor to realize upon his security by a judicial sale is a substantive right of property guaranteed by the Fifth Amendment.

"The contention, however, attributes to the Radford decision a scope broader than warranted by the facts of the case or by the language of the opinion. Neither in word nor in effect did the court there hold that a mortgagee's right to a judicial sale was a right of property beyond the power of equitable modification. On the contrary, the court remarked (page 597) upon the power of equity to permit a receivership to continue

'to prevent a sacrifice of the creditor's interest.' The modification imposed by the Frazier-Lemke Act there under consideration was held to be confiscatory because designed to promote the interests of the mortgagor at the expense of the mortgagee.

"The contention, moreover, rests upon inverted reasoning. For let it be granted that the right of a mortgagee to a judicial sale is a property right under the local law. Nevertheless, if a judicial sale is found to be inadequate fully to protect the mortgagee's right, under a familiar principle equity may interpose to prevent a sacrifice thereof. And it is in the discharge of this responsibility that courts of equity have developed the device of an upset price. Thus in cases in which, due to the size or spread or character of the property which is the subject-matter of the sale, a public offering may not reasonably be expected to realize any bids whatever commensurate to the value of the property, the chancellor errs if he fails to protect the mortgagee by an adequate upset price. *First National Bank* v. *Flershem, supra.*

"In such a case, the bare legal right of the mortgagee to a judicial sale is superseded not by the confiscation of the unavailing right that was his, but rather by the more effective process of equity which assures to the mortgagee the essential substance of his right. In no sense can the addition of the equitable remedy be deemed to impair the effect of the creditor's contract. *National Surety Co.* v. *Architectural Decorating Co.*, 226 U. S. 276; *Water Works Co.* v. *Oshkosh*, 187 U. S. 437; *Bernheimer* v. *Converse*, 206 U. S. 516. When thus viewed in its true perspective, the equitable power is seen to be not a species of confiscation but the very antithesis thereof.

"Especially is this conclusion applicable in proceedings for the reorganization of a railroad. For under the law of the land, railroad properties are not subject-matter for unrestricted bargain and sale. Thus, under the Interstate Commerce Act, as amended, especially by the Act of June 16, 1933, 48 Stat. 217, 49 U. S. C. A. Section 5, the purchase or other acquisition of railroad property subject to the Interstate Commerce Act has been subjected to the regulation of the Interstate Commerce Commission. And in determining whether or not a given purchase shall be authorized, it is the func-

tion of the Commission not to boost the purchase price for the benefit of those having private rights in the property, but to determine whether the purchase 'will promote the public interest' and 'will be in harmony with and in furtherance of the plan for the consolidation of railway properties established' or to be established by it pursuant to said Act. Moreover, unless the prospective purchaser has sufficient ready cash to consummate the acquisition, under Section 439 of the Transportation Act of 1920, 49 U. S. C. A. 20a it can make good its bid only if the Commission approves its corporate financing undertaken to that end. Plainly, a judicial sale of such property, even though the sale be public in form, will not give free play to the process of competitive bidding. It follows that one having a lien upon railroad property is in a particularly unfavorable position to claim that the interposition of the beneficent powers of equity have 'deprived' him of anything of value.

"In reorganization proceedings, the distinction between public utilities and other corporations or individuals seems to have been recognized, if not directly adjudicated, by the Supreme Court. *First National Bank* v. *Flershem*, 290 U. S., note 7 beginning at page 515; *Continental Bank* v. *Rock Island R. R.* 294 U. S. 648; *Kansas City Rwy.* v. *Central Union Trust Co.*, 271 U. S. at page 455. The distinction may further serve to differentiate the Radford case having to do with the disposition of farm property from a proceeding for the reorganization of a railroad.

"From the foregoing considerations I incline to the view that a District Court of the United States in a proper case may in the exercise of its inherent equity powers approve and enforce a plan of reorganization for a railroad without resort to the fiction of a judicial sale. That being so, it follows that the provision of subdivision (e) now under attack serves merely to confer upon the District Court in its bankruptcy part a power theretofore existing in its equity part. It is too late now to question the power of Congress to confer equity powers upon the bankruptcy court, and I hold the questioned provision to be valid and constitutional."

APPENDIX B.

(Being Sections 16, 18 and 20 of Chap. 77, Ill. St. Bar Stats. 1935.)

"16. *Certificate of sale.* When any real estate is sold by virtue of an execution, judgment, or decree of foreclosure of mortgage, or enforcement of mechanic's lien, or vendor's lien, or for the payment of money, it shall be the duty of the sheriff, master in chancery or other officer, except as otherwise in this Act provided, instead of executing a deed for the premises sold, to give to the purchaser a certificate describing the premises purchased by him, showing the amount paid therefor, or if purchased by the person in whose favor the execution is taken or decree is entered, the amount of his bid, the time when the purchaser will be entitled to a deed, unless the premises shall be redeemed, as provided in this Act."

* * * * * *

"18. *Redemption by defendant or his privies.* Any defendant, his heirs, executors, administrators, assigns, or any person interested in the premises, through or under the defendant, may, except as to any sale had by virtue of decree of foreclosure of mortgage made by a corporation wherein right of redemption shall be waived, as in section 18a of this Act provided, within twelve months from said sale, redeem the real estate so sold by paying to the purchaser thereof, his executors, administrators or assigns or to the sheriff or master in chancery, or other officer who sold the same, or his successor in office, for the benefit of such purchaser, his executors, administrators, or assigns, the sum of money for which the premises were sold or bid off, with interest thereon at the rate of six per centum per annum from the time of such sale, whereupon such sale and certificate shall be null and void."

* * * * * *

"20. *Redemption by creditor.* If such redemption is not made, any decree or judgment creditor, his heirs, executors, administrators or assigns may, after the expiration of twelve months and within fifteen months after the sale, and when any sale is had under any order or decree of foreclosure upon a mortgage or trust deed executed by a corporation and containing a waiver of the right of redemp-

tion any decree or judgment creditor of such corporation may within three months after the sale, redeem the premises in the following manner: Such creditor, so entitled to redeem, his heirs, executors, administrators or assigns may sue out an execution upon his judgment or decree, and place the same in the hands of the sheriff or other proper officer to execute the same, who shall endorse upon the back thereof a levy of the premises desired to be redeemed; and the person so entitled and desiring to make such redemption shall pay to such officer the amount for which the premises to be redeemed were sold, with interest thereon at the rate of six per centum per annum from the date of the sale, for the use of the purchaser of such premises, his executors, administrators or assigns, whereupon such officer shall make and file in the office of the recorder of the county in which the premises are situated a certificate of such redemption, and shall advertise and offer the premises for sale under said execution as in other cases of sale or execution."

FILED
OCT 22 1936
CHARLES ELMORE CROPL
CLERK

In the

Supreme Court of the United States

October term, A. D. 1936.

No. 271

In the matter of 620 CHURCH STREET BUILDING CORPORATION, a corporation, debtor under section 77B of the bankruptcy act.

620 CHURCH STREET BUILDING CORPORATION, IRENE K. GOODMAN, G. WALLER, M. LONG, A. W. KIBBY, EMIL ROSENTHAL AND B. K. GOODMAN,

petitioners,

vs.

WARNER G. BAIRD, trustee of debtor, CHESTER R. DAVIS, MURRAY WOLBACH AND JAMES R. MCCAHEY, as members of bondholders committee for the holders of first mortgage bonds, LOUIS M. QUITMAN AND EDGAR N. GREENEBAUM, as trustees under first mortgage, WILLIAM L. O'CONNELL, as receiver of Central Republic Trust Company, CLARA ABT, LUCILLE ABT, EDWARD SCHOEN AND ALICE G. HIRSH,

respondents.

On writ of certiorari to the Circuit Court of Appeals for the Seventh Circuit.

Brief for the respondents Louis M. Quitman and Edgar N. Greenebaum, first mortgage trustees.

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In the

Supreme Court of the United States

October term, A. D. 1936.

No. 271

In the matter of 620 CHURCH STREET BUILDING CORPORATION, a corporation, debtor under section 77B of the bankruptcy act.

620 CHURCH STREET BUILDING CORPORATION, IRENE K. GOODMAN, G. WALLER, M. LONG, A. W. KIBBY, EMIL ROSENTHAL AND B. K. GOODMAN,

petitioners,

vs.

WARNER G. BAIRD, trustee of debtor, CHESTER R. DAVIS, MURRAY WOLBACH AND JAMES R. MCCAHEY, as members of bondholders committee for the holders of first mortgage bonds, LOUIS M. QUITMAN AND EDGAR N. GREENEBAUM, as trustees under first mortgage, WILLIAM L. O'CONNELL, as receiver of Central Republic Trust Company, CLARA ABT, LUCILLE ABT, EDWARD SCHOEN AND ALICE G. HIRSH,

respondents.

Brief for the respondents Louis M. Quitman and Edgar N. Greenebaum, first mortgage trustees.

STATEMENT OF THE CASE.

Grant of certiorari:

The order granting certiorari in this case (October 12, 1936) provided that the case be advanced for hearing immediately following no. 48, *Tennessee Publishing Company* v. *American National Bank, et al.* (R. 29.)

Errors assigned by petitioners:

Petitioners do not question the regularity or propriety of any of the proceedings and orders in this case prior to the entry of the order of March 31, 1936, confirming the plan of reorganization. Thus it is undisputed (1) that the debtor's voluntary petition for reorganization under section 77B of the bankruptcy act was properly filed under the statute, in good faith (R. 12—par. 1); (2) that the court acquired jurisdiction in this proceeding of the debtor and its property, all its creditors and stockholders (R. 12—par. 1); (3) that possession of the debtor's property—two leasehold estates and the improvements thereon, comprising the "Carlson Building Annex," in Evanston, Illinois—was in the hands of the trustee appointed in this proceeding (R. 7—par. 5); (4) that the petitioners, other than the debtor corporation, came into the proceeding to obtain allowance of their respective claims, to-wit, some as class 3 claims (on second mortgage notes), some as class 4 (on third mortgage notes), some as class 5 claims (stockholders) (R. 7—par. 4; R. 13—par. 3).

The errors assigned by petitioners (R. 18-20) are directed to the following findings and orders embraced in the confirmation decree:

> "5. That the committee acting under the deposit agreement dated December 12, 1929, referred to above, is lawfully constituted, and that the said committee has full power, right and authority to consent to and accept the plan for and on behalf of each of the holders of Carlson Annex bonds deposited with said committee under said deposit agreement; that the committee has accepted the plan in writing on behalf of the holders of all Carlson Annex bonds on deposit with it under said deposit agreement, to-wit: on behalf of the holders of $371,300 principal amount of said bonds with interest thereon, which amount is in excess of 66-2/3% of the aggregate amount of allowed claims of class 2, and such consent and acceptance so filed by the committee is hereby declared to constitute

the consent and acceptance of the plan by the holders of the certificates of deposit issued under said deposit agreement in respect of said Carlson Annex bonds on deposit with the committee thereunder." (R. 14.)

"11. That the court having heard evidence and testimony on the value of the property of the debtor finds: that the principal property of the debtor consists of the two leasehold estates and improvements on the property located at 620 to 628 Church Street, in the City of Evanston, County of Cook, and State of Illinois, said two leasehold estates, together with all improvements thereon and appurtenances thereto, being more specifically described in the plan and being hereinafter sometimes referred to as the 'Carlson Building Annex'; that the Carlson Building Annex has a fair market value of $245,025, and that there is no equity over and above the $445,500 principal amount of Carlson Annex bonds outstanding against the Carlson Building Annex; that the debtor is accordingly insolvent; that the stockholders are not entitled to participate in the plan, and that their acceptance of the plan is not a prerequisite to the confirmation of the plan." (R. 15.)

"12. That based on the abovementioned evidence and testimony concerning the value of the Carlson Building Annex, the court has appraised and does hereby appraise all claims allowed in class 3 and class 4 to be of no value, there being no equity in the Carlson Building Annex bonds outstanding against the Carlson Building Annex, and accordingly no securities, cash or any other thing of value shall be distributed under the plan in respect of any of the claims allowed in classes 3 and 4, and the acceptance of the plan by the holders of such claims is not a prerequisite to the confirmation of the plan. The court further finds that the foregoing method of treatment of the holders of claims in classes 3 and 4 provides adequate protection for the realization by the holders thereof of the value thereof under and consistent with the circumstances of the case, the same being of no value." (R. 15.)

"13. That the plan has been accepted as required by the provisions of subdivision (e) of section 77B of the Act to Establish a Uniform System of Bankruptcy throughout the United States as amended (hereinafter referred to as the 'Bankruptcy Act'), and the above described acceptances have been filed in this proceeding." (R. 15.)

"15. That the plan is fair, equitable, and feasible, and does not discriminate unfairly in favor of any class or classes of creditors or stockholders." (R. 16.)

"20. That all provisions of the bankruptcy act which ought to be complied with prior to the confirmation of the plan have been fully complied with in the manner provided therein." (R. 16.)

"21. That all objections to the plan, oral or written, are hereby overruled, and the plan is hereby in all respects finally approved and confirmed." (R. 16.)

"22. That the provisions of the plan and of this order shall be binding upon the debtor, all of its stockholders, including those who have not as well as those who have accepted the plan, and all creditors of the debtor, secured or unsecured, whether or not affected by the plan, and whether or not their claims have been filed, and if filed whether or not allowed, including creditors who have not as well as those who have accepted the plan." (R. 16.)

The errors assigned by petitioners, though seventeen in number (R. 18-20), present only two distinct propositions:

(1) That the district court erred in finding that the fair market value of debtor's property is $245,025; and that consequently (a) there is no equity over the principal amount of the outstanding first mortgage bonds ($445,500);* (b) the debtor is insol-

*The first mortgage indebtedness includes interest from January 1, 1931; at 6% to date of confirmation decree—ignoring the 7% rate applicable after default—equals $144,332.50. This brings the total to $585,832.50, without taking account of the expenses of litigation and other accrued charges under the first mortgage.

vent; (c) the class 3 and class 4 claims are valueless.

(2) That, notwithstanding these circumstances, the district court erred in decreeing that junior claimants were not equitably entitled to apportionment of any cash or securities under the plan of reorganization and their consent was not a prerequisite to confirmation of the reorganization plan.

Value of property and claims:

The Circuit Court of Appeals, in its memorandum on the petition for appeal, said (R. 21):

> "In view of the fact that, upon what must have been a full hearing as to value of the premises, the court made a specific finding as to that value, this court would have no right to disturb that finding."

We remind the court that the petition for leave to appeal from the decree of the district court was filed under section 24(b) of the bankruptcy act, pursuant to which the Circuit Court of Appeals could exercise jurisdiction only "to superintend and revise in matter of law." No claim is made by any assignment of error that the petitioners were denied a fair and adequate hearing as to the value of debtor's property and of petitioners' claims. No question of law is raised with respect to any incident of this hearing.

Confirmation of plan without petitioners' consents:

Thus the case narrows down to a single point. Value or no value, is the consent of junior claimants of various classes an indispensable prerequisite to confirmation of a plan of reorganization by a court of bankruptcy, exercising jurisdiction under section 77B of the bankruptcy act, when after a fair hearing it has been determined that such claims are valueless? Or, lacking such consents, must the court reject reorganization for the benefit of senior lienors and abandon its jurisdiction (so that, as petitioners assume,

the first mortgage bondholders will be compelled to resort to a foreclosure sale under state law, with attendant rights of redemption)?

Contentions of respondents:

(1) The benefits of a reorganization plan under section 77B need not extend to all classes of creditors and stockholders, if the liabilities of the debtor corporation exceed its assets, but only to those equitably entitled to participate, according to the amount, quality and priority of their respective claims.

(2) Subsection (b) of section 77B*—more particularly, subparagraph (4) and subparagraph (5) (c) and (d) of subsection (b)—as applied in this case, does not deprive petitioners of property without due process of law.

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*Quoted in Appendix, p. 22.

SUMMARY OF ARGUMENT.

I.

Since an appeal under section 24(b) of the bankruptcy act is confined to questions of law, the Circuit Court of Appeals properly held (R. 21) that—with no challenge to the fairness or adequacy of the hearing as to the value of debtor's property and petitioners' claims—the correctness of the valuation arrived at by the district court is not reviewable.

In re Loving, 224 U. S., 183, 188-189, 56 L. ed. 725, 726-727.

Elliott v. Toeppner, 187 U. S. 327, 334, 47 L. ed. 200, 203.

II.

Reorganization under section 77B of the bankruptcy act is not limited—either (a) by statutory formula, or (b) by demands of equity, or (c) by constitutional mandate—to a plan extending participation to all classes of creditors and stockholders, when the liabilities of the debtor corporation exceed its assets.

Section 77B of the bankruptcy act, subsection (b)—(1), (2), (4), (5), (9); also subsection (e) (1) (11 U.S.C. section 207, subsections as above).*

In re Central Funding Corp. (CCA 2), 75 F. (2d) 256, 259-260.

In re Mortgage Securities Corp. (CCA 2), 75 F. (2d) 261.

In re Reading Hotel Corp. (D.C., E.D. Pa.), 10 F. Supp. 470.

In re William Penn Garage (D. C., W. D. Pa.), Commerce Clearing House Bankruptcy Law Service, ¶3649.

See also cases cited under Points III, IV and V, *infra.*

*Quoted in Appendix, pp. 22-24.

III.

Exercise of bankruptcy jurisdiction in a manner that disposes of the property of the bankrupt (or "debtor" under section 77B) without foreclosure sale and attendant rights of redemption under state law, does not violate the due process provision of the fifth amendment.

Van Huffel v. Harkelrode, 284 U. S. 225, 227-228, 76 L. ed. 256, 259 (sale in bankruptcy free and clear of liens, under Act of 1898).

Ray v. Norseworthy, 23 Wall. (90 U. S.) 128, 23 L. ed. 116 (sale in bankruptcy free and clear of liens, under Act of 1867).

Houston v. City Bank of New Orleans, 6 How. (47 U. S.) 486, 506, 12 L. ed. 526, 534 (sale in bankruptcy free and clear of liens, under Act of 1841).

Dugan v. Logan, 229 Ky. 5, 16 S. W. (2d) 763; cert. den. 280 U. S. 587.

American Mines Equipment Co. v. Illinois Coal Corp. (CCA 7), 31 F. (2d) 507, 510-513; cert. den. 280 U. S. 572, 74 L. ed. 624 (sale by federal court without right of redemption, under general creditors' bill filed with debtor's consent).

In re Novak (D.C., N.D. Ia.), 111 Fed. 978 (no right of redemption from trustee's sale in bankruptcy).

Brown v. Timmons, 79 Mont. 246, 256 Pac. 176, 178-179 (bankrupt's right of redemption from foreclosure sale by state court passed to trustee in bankruptcy).

In re Central Funding Corp. (CCA 2), 75 F. (2d) 256, 260-261.

In re New York, New Haven & Hartford Rd. Co. (D. C. Conn.—Sept. 15, 1936), Commerce Clearing House Bankruptcy Law Service, ¶4172.

IV.

Although it is stated in the opinion of this court in Louisville Joint Stock Land Bank v. Radford, 295 U. S. 555, that "by the settled practice, a sale free of liens will not be ordered by the bankruptcy court if it appears that the amount of the incumbrance exceeds the value of the property," this refers to ordinary bankruptcy liquidation proceedings and not to reorganization proceedings under section 77B; and moreover, does not deny the power of a bankruptcy court, under appropriate circumstances, to order such sale regardless of the value of the property.

In re Franklin Brewing Co. (CCA 2), 249 Fed. 333, 335.

In re Union Trust Co. (CCA 1), 122 Fed. 937, 939, 940.

In re Roger Brown & Co. (CCA 8), 196 Fed. 758, 761.

In re Throckmorton (CCA 6), 196 Fed. 656, 659.

In re Hasie (D.C. Tex.), 206 Fed. 789, 792.

In re Theiberg (D.C., N.J.), 280 Fed. 408.

In re Loveland (CCA 1), 155 Fed. 838, 839.

In re Central Funding Corp. (CCA 2), 75 F. (2d) 256, 260-261.

V.

It is no longer open to dispute that the power of Congress to legislate on the subject of bankruptcies includes the power to bring within the bankruptcy jurisdiction the subject of corporate reorganizations. Such jurisdiction is not rendered unconstitutional because it extends to secured claims against the debtor and its property as well as unsecured claims; nor because it provides remedies for the ascertainment and enforcement of pre-existing lien claims other than those provided by state law—remedies affording substantially equivalent benefits.

Continental Illinois National Bank & Trust Co. v. C. R. I. & P. Ry. Co., 294 U. S. 648, 667-675, 79 L. ed. 1110, 1123-1127.

Campbell v. Allegheny Corp. (CCA 4), 75 F. (2d) 947, 951-955; cert. den. 296 U. S. 581, 80 L. ed. 104.

In re Landquist (CCA 7), 70 F. (2d) 929, 933; cert. den. 293 U. S. 584, 79 L. ed. 680.

Hanover National Bank v. Moyses, 186 U. S. 181, 46 L. ed. 1113.

Ex parte City Bank of New Orleans, 3 How. (44 U. S.) 292, 316, 11 L. ed. 603, 614.

Nugent, Assignee, v. Boyd, 3 How. (44 U. S.) 426, 437, 11 L. ed. 664, 669.

McRaney v. Riley, 128 Miss. 665, 91 So. 399, 400-402.

In re Jersey Island Packing Co. (CCA 9), 136 Fed. 625, 627.

In re New York, New Haven & Hartford Rd. Co. (D.C. Conn.), Commerce Clearing House Bankruptcy Law Service, ¶4172, at pp. 2161-2162.

ARGUMENT.

The correctness of the trial judge's valuation of debtor's property and of petitioners' claims is not reviewable.

Petitioners, in conformity with section 24(b) of the bankruptcy act, petitioned the Circuit Court of Appeals "that they may be allowed, in the discretion of this honorable court, to appeal in matter of law herein." (R. 9.)

The scope of such appeal, if granted, is strictly limited to questions of law (*In re Loving,* 224 U. S. 183, 188-189; *Elliott* v. *Toeppner,* 187 U. S. 327, 334.)

With no challenge to the fairness of the hearing on the value of debtor's property and of petitioners' claims, no contention that incompetent evidence was received or competent evidence excluded, the Circuit Court of Appeals correctly concluded that it would have no right to disturb the trial judge's finding of value. (Memorandum denying appeal, *supra,* p. 5.)

II.

Reorganization under Section 77B need not extend participation to all classes of creditors and stockholders, when liabilities of debtor corporation exceed assets.

The text of the statute, quoted at pp. 22-24 *infra,* leaves no doubt of the intention to provide for a reorganization such as that accomplished in this case, namely: a transfer of the Carlson Annex leaseholds, held by the 620 Church Street Building Corporation, to the 636 Church Street Building Corporation, holder of the adjoining Carlson Building leasehold, and issuance to the holders of Carlson Annex bonds of (a) $222,850 new first mortgage bonds out of $684,750 to be secured by the combined leaseholds, also (b) 25% of the common stock of the new owner corporation.* A complementary plan of reorganization of the 636

*The new bonds allocated to the Carlson Annex bondholders represents 50% of the face amount of their old bonds; the stock, one share per $500 old bond.

Church Street Building Corporation was consummated in another section 77B proceeding in the same court. (R. 7-8, par. 9.)*

No question is raised as to the regularity of the proceedings in this case up to the point of entry of the decree confirming the plan of reorganization. At this stage of the proceedings—in a case where the fair market value of the debtor property is but 40% of the first mortgage indebtedness—challenge comes only from claimants whose interest in the debtor's property are indisputably inferior to the interest of the first mortgage bondholders.

Manifestly, if under the circumstances of this case a reorganization under section 77B could not apportion all of the debtor's property to the senior claimants, in accordance with elementary precepts of equity, the statute would be of no avail in this case and many similar cases. Instead, the "nuisance values" and "maneuvering values" by means of which unjust toll was commonly exacted as part of the price of corporate reorganization through equity receivership proceedings, or kindred proceedings, would continue to thrive.

As stated by Circuit Court of Appeals for the Second Circuit, in upholding a reorganization under section 77B for the benefit of first mortgage bondholders only, where essentially all that was accomplished was to defer liquidation of the collateral securing the first mortgage bonds (*In re Central Funding Corp.*, 75 F. (2d) 256):

> "The most flagrant occasion for a reorganization is where only creditors' rights are to be adjusted, and liquidation is to be slow enough to take advantage of market conditions obtaining over a long period. Section 77B expressly provides for such situations as we

*The Carlson Building is a 9-story office and store building at the southeast corner of Orrington avenue and Church street, Evanston, Illinois. The Carlson Annex is a part 7-story and part 2-story office and store building adjoining the corner building to the east of Church street. The Annex has no independent heating plant, elevators, or entrance lobby, but avails itself (under operating contract) of these facilities of the corner building.

have here, and they are proper subjects of bankruptcy legislation. To restrict the Act to reorganizations where the debtor has an equity would be to deprive the section of much, if not most, of its usefulness." (p. 261.)

"We cannot, however, doubt that it is within the general meaning of the term 'reorganization'. In common parlance that term is not limited to cases where the rights of all persons interested in a corporation, whether lienors, general creditors or stockholders, are made to survive under some new corporate arrangement. Not infrequently the rights of some of these classes have become so worthless that they deserve and receive no recognition in the reorganization." (p. 259.)

Under paragraph (4) of subsection (b) of section 77B, if the judge determines that the debtor is insolvent, no provision need be made in the plan of reorganization for stockholders. Under paragraph (5) of subsection (b), if two-thirds of any class of creditors do not accept the plan, the plan must provide "adequate protection" for the realization of the value of the interest, claim, or lien of such class in debtor's property, through (a) continued subjection of the property to such interest or lien, or (b) sale free of such interest or lien at fair upset price, or (c) appraisal of such interest or lien and payment of appraised value in cash, or (d) by such method as, in the opinion of the judge, under the circumstances of the particular case, will equitably provide such "adequate protection."*

The court's finding of insolvency obviated any need to make provision, under the plan confirmed in this case, to protect the interest of stockholders. "Adequate protection" of the interests, claims and liens of the second and third mortgage noteholders was afforded under the plan by providing for appraisal of the value of these claims, such value to be paid in cash.

*Text of statute, *infra*, p. 22.

Naturally, with first mortgage indebtedness two and one-half times the value of debtor's property, it was undoubtedly anticipated by the proponents of the plan that appraisal would yield no cash to the junior creditors. But if the "adequate protection" afforded by the plan yielded nothing to the second and third mortgage noteholders, this result was caused not by the plan, nor by the court's decree, nor by the enactment of section 77B, but by misjudgment in the original investment represented by these junior claims, or if the original investment was sound to subsequent retrogression due to the turn of economic events. If, in the apportionment of assets consistent with equitable priorities, a court of bankruptcy turns away some claimants empty-handed, this is not a deprivation of property without due process of law. Rather, it is of the essence of bankruptcy process, of which one of the main objectives —formerly the sole objective—is the distribution of the debtor's assets to its creditors in measure with the quality and quantity of their claims.

We quote from the opinion of the Circuit Court of Appeals for the Fourth Circuit in *Campbell* v. *Allegheny Corporation*, 75 F. (2d) 947, at pp. 953-954:

> "Little need be said as to the question which arises under the fifth amendment. There is no question, of course, but that the exercise of the bankruptcy power by Congress, as is the case with other delegated powers, is subject to the requirement of due process contained in that amendment. *Monogahela Nav. Co.* v. *U. S.*, 148 U. S. 312, 336, 13 S. Ct. 622, 37 L. Ed. 463; *Hanover Nat. Bank* v. *Moyses, supra*, 186 U. S. 181, 192, 22 St. Ct. 857, 862, 46 L. Ed. 1113. But as any exercise of the bankruptcy power impairs the obligation of contracts, such impairment is not to be taken as in itself a denial of due process. For the provisions of the act to violate the amendment, they must be so grossly arbitrary and unreasonable as to be incompatible with fundamental law. *Hanover Nat. Bank* v. *Moyses, supra.* We do not think that the requirement

that secured creditors scale their debts in accordance with a plan which two-thirds of them are willing to accept and which has been approved by the court as reasonable and fair, and accept in lieu of payment in money such securities as are specified in the plan, can be said to be such an arbitrary and unreasonable exercise of the bankruptcy power as to amount to a denial of due process.

The fact that secured debts are affected by the act does not, of course, raise any grave constitutional question, and can be dismissed with brief comment. "A secured debt or lien is, so far as the Constitution of the United States is concerned, a no more sacred kind of property than an unsecured debt. * * * And the Constitution expressly permits and grants to Congress the exercise of the power to affect such property, whether it be an unsecured debt or whether it be a lien, by laws relating to 'subject of bankruptcies.'" In re Burgh (D. C.), 7 F. Supp. 184, 185.

As a matter of fact, no property in any real sense is taken from the dissenting creditor when he is compelled under section 77B to scale his claim and accept securities in lieu thereof. The securities held by him have already shrunk in value before the proceeding under the act is instituted; and all that is required of him is that he face reality and accept his pro rata interest in the debtor's property in a form which will not jeopardize the rights of other creditors similarly situated. If he were allowed to insist on the foreclosure of the lien in which he is interested in common with others, he would bring serious injury to them without benefit to himself. Under the act, he is merely required to accept what two-thirds of those similarly situated are willing to accept, and what the court has found to be fair and reasonable under the circumstances; and, when the situation is viewed realistically, it is readily seen that he is not required to surrender any part of the value either of his securities or of the property available for the payment of his claim. What he in fact gives up is merely the arbitrary power to frustrate the wishes of the great majority of those who have a common interest in the property of the debtor, or, in other words, the power to demand from other creditors an

unconscionable settlement of his claim as the price of withdrawing objection to a plan of reorganization which is fair to all parties concerned.

The act is based upon an equitable recognition of the rights of all who have an interest in a common property, and is in accord with the principle under which courts of equity have denied to dissenting creditors the right to prevent the consummation of a plan of reorganization which has been found to be fair and open to all creditors on the same terms. See *Fearon* v. *Bankers' Trust Co.* (C. C. A. 3), 238 F. 83; *Simon* v. *New Orleans R. Co.* (C. C. A. 5), 242 F. 62. It embodies substantially the principles of corporate reorganization adopted in England and Canada many years ago, and, as shown above, held reasonable by the Supreme Court in the case of *Canadian Southern Ry. Co.* v. *Gebhard, supra,* where the court said: 'In no just sense do such governmental regulations deprive a person of his property without due process of law.' "

In the reorganization of the Reading Hotel Corporation under section 77B, approved by the District Court for the Eastern District of Pennsylvania (10 F. Supp. 470), the master found the debtor "definitely and hopelessly insolvent." The stockholders, on exceptions to the master's report, contended that the master erred in failing to take account of "a potential value which is really based upon a guess (perhaps not altogether unjustified) that the hotel by reason of past history of wide advertisement, good management, and excellent reputation will, when times improve, make money for its then owners." The court held, however, that there was nothing in section 77B which justified such an interpretation of the statute, or changed the original definition of insolvency. To the argument of the stockholders that section 77B was passed for the relief of debtors, and that unless some recognition were given to the interests of stockholders a reorganization under section 77B in the case of an insolvent corporation with a mortgage indebtedness would amount to nothing more than foreclos-

ure with possible readjustment of interests among various classes of creditors, the court responded (p. 471):

> "The insolvency of the debtor corporation eliminates the necessity for acceptance by a majority of stockholders as a prerequisite to the confirmation of the plan. It also eliminates the necessity of making provision for dissenting stockholders in the plan. But when subsection (b) (4) speaks of providing for stockholders, the provision it refers to is 'adequate protection for the realization by them of the value of their equity.' Obviously, if there is no equity, there is nothing which can be 'realized,' and the stockholders are not entitled to any of the alternatives such as sale of the property or cash payments, which they would have if their holdings had a present cash value."

III and IV.

Bankruptcy distribution of debtor's property without foreclosure sale and rights of redemption does not violate the due process provision of the fifth amendment.

The petition for certiorari in this case stresses mainly the rights of junior lienors: the right to insist upon a public sale, the right to bid at such sale, the right of redemption within fifteen months. (Petition, p. 28.) Of the right to redeem, petitioners say: "Whether valuable or not from a monetary standpoint, however, it is absolute and vested and it is not for the court to put a price upon it or to declare it valueless." (Petition, p. 33.)

It is by no means a self-evident postulate, as assumed by petitioners, that in default of reorganization under section 77B the debtor's property would be disposed of by foreclosure sale, and that some of the petitioners would thereupon become vested with the right to redeem from such sale within fifteen months. Other methods of liquidation of the debtor's property, without rights of redemption, are illustrated by the cases cited at pp. 8-9, *supra* (under points III and IV). These methods include sale in bank-

ruptcy liquidation free and clear of liens; sale free of redemption rights in a federal equity receivership proceeding; sale free of redemption rights in equivalent state court corporate liquidation proceedings.

In neither the 1841, 1867 or 1898 bankruptcy acts do we find any express grant of power to courts of bankruptcy to sell mortgaged property free and clear of liens; in each of these acts, at the same time, we find (in varying form) an express declaration that valid mortgages and liens on the debtor's property shall not be affected, if not fraudulent or preferential; yet under each of these acts the power to sell the debtor's property free and clear of liens has been recognized as implicit in the general grant to the courts of bankruptcy of all equitable powers essential to the proper administration and distribution of insolvent estates. Under the act of 1841: *Ex parte The City Bank of New Orleans,* 3 How. 292, 11 L. ed. 603; *Nugent, Assignee,* v. *Boyd,* 3 How. 426, 11 L. ed. 664; *Houston* v. *City Bank of New Orleans,* 6 How. 504, 12 L. ed. 426. Under the act of 1867: *Ray* v. *Norseworthy,* 23 Wall. 128, 23 L. ed. 116. Under the act of 1898: *Van Huffel* v. *Harkelrode,* 284 U. S. 225, 76 L. ed. 256; *In re Union Trust Co.* (C. C. A. 1), 122 Fed. 937; additional cases cited under point IV, *supra,* p. 9.

While it may well be "the settled practice" in general bankruptcy not to sell property free and clear of liens unless it is fairly anticipated that the sale will produce a margin over the lien indebtedness, it has often been declared that this is a rule of policy, and not a delimitation upon bankruptcy jurisdiction. (See cases cited at p. 9, *supra,* under point IV.)

But even if it is assumed that the only alternative to reorganization under section 77B is reversion to the foreclosure suit suspended by the institution of this proceeding, and that a foreclosure sale of the debtor's leaseholds would vest in some of the petitioners the right to redeem, it is a distortion of the decision of this court in *Louisville Joint*

Stock Land Bank v. *Radford* to say that the bankruptcy power transgresses the due process of law, in contravention of the fifth amendment, when it produces such a result. It is the ordinary and inherent routine of bankruptcy jurisdiction to divest property rights. The difficulty encountered in the *Radford* case was not merely that the mortgagee was to recover less than its due from an insolvent debtor. The mortgaged farm was not to be sold or conveyed for the benefit of the mortgagee (and other creditors, if the proceeds of the sale exceeded the mortgage), but to be restored to the mortgagor on a rental basis for a span of five years, subject meanwhile to an option in the mortgagor to dispose of the mortgage indebtedness at less than half its amount.

The *Radford* case, with its forceful insistence that the mortgagor could not be thus indulged at the expense of the mortgagee, after default had ripened the mortgagee's right to satisfy its claim out of the mortgaged property, is strong authority against the contention of petitioners in this case. The rights of petitioners are not cut down by section 77B of the bankruptcy act, but fully recognized and preserved. All that happened, in consequence of debtor's resort to bankruptcy jurisdiction under section 77B, was a change of forum and procedure, but not interposition of a new measure of rights. It is elementary that bankruptcy may supplant any and all modes of procedure provided by state law for the enforcement of the obligations of a debtor in failing circumstances. "It is, in short, a system of laws to take care of the rights of the parties interested, when a business failure supervenes." (Remington on Bankruptcy, 4th ed. v. I, p. 47.)

V.

The power of Congress to legislate on the subject of bankruptcies may properly extend to secured claims against the debtor's property as well as unsecured claims; and may provide remedies for the ascertainment and enforcement of pre-existing lien claims other than those provided by state law, provided such remedies afford substantially equivalent benefits.

Petitioners do not question the general validity of section 77B as a code of procedure for the reorganization of financially embarrassed or insolvent corporations; nor that such reorganization may deal with claims secured by liens on the debtor's property as well as unsecured claims. The petitioner corporation itself initiated this proceeding for reorganization; the petitioners who hold second or third mortgage notes of the debtor corporation came into the proceeding to prove their claims—and, if possible, to persuade the first mortgage bondholders voluntarily to yield to them some share in the reorganization, despite the great disparity between the first mortgage indebtedness and the value of the debtor property. (R. 7—pars. 7 and 8.)

Because their claims were worthless *ab initio*, or have been rendered worthless by the course of events, the procedure provided by section 77B has brought petitioners no cash or substituted securities. Not by legislative or judicial fiat that they shall take less than their due, but by orderly and fair ascertainment of what is justly recoverable on their claims upon general distribution of the insolvent debtor's assets. Petitioners protest that, as the matter has turned out, they might be better off if the first mortgage bondholders were denied the facilities and economies of reorganization procedure under section 77B and remitted to foreclosure under state law. If so, it is not because of any showing that prolongation of the litigation for another year or more would increase the value of debtor's property from $245,025 to something over $600,000, the approximate first mortgage indebtedness at this time with-

out reckoning accrued and future costs of litigation. Reduced to its ultimate essence, the true complaint of petitioners is that section 77B, as applied in this case, has deprived them of such maneuvering advantages as they might have had under the inefficient and unduly costly modes of procedure for corporate reorganization which section 77B was designed to supplant. It would be anomalous, indeed, if equity or the constitutional requirement of due process could reasonably be found to support a contention so flagrantly at odds with justice and good conscience.

Not to elaborate upon what this court has said about the nature and scope of the bankruptcy power (cases cited at pp. 9-10, *supra*), we submit that this great and beneficent power conferred on Congress by the federal constitution has not been unconstitutionally exercised in the enactment of section 77B of the bankruptcy act, or any of the subdivisions thereof herein involved; that in the application of section 77B in this case no inequity has resulted to the petitioners, or any of them; that the first mortgage bondholders, through the reorganization confirmed by the court, will receive no more than their equitable due as the holders of obligations secured by superior lien on the debtor's property. Wherefore, these respondents urge that the Circuit Court of Appeals did not err in denying to petitioners leave to appeal, and that said order of the Circuit Court of Appeals and the decree of the District Court should be affirmed.

Respectfully submitted,

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APPENDIX.

Section 77B of Bankruptcy Act, 11 U. S. C. Section 207.

Subsection (b):

"A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character or otherwise; * * * (4) shall provide in respect of each class of stockholders, of which less than a majority shall accept such plan (unless the judge shall determine either that the debtor is insolvent, or that the interest of such class of stockholders will not be affected adversely by the plan), adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with by the plan, either, as provided in the plan, (a) by a sale of the property at not less than a fair upset price, or (b) by appraisal and payment in cash of the value either of their stock, or at the objecting stockholders' election, of the securities allotted to such stockholders under the plan, if any shall be so allotted, or (c) by such methods as will do substantial justice to such stockholders under and consistent with the circumstances of the particular case; (5) shall provide in respect of each class of creditors of which less than two thirds in amount shall accept such plan (unless the claims of such class of creditors will not be affected by the plan, or the plan makes provision for the payment of their claims in cash in full), provide adequate protection for the realization by them of the value of their interests, claims, or liens, if the property affected by such interests, claims, or liens is dealt with by the plan, either, as provided in the plan, (a) by the transfer or sale of such property subject to such interests, claims, or liens, or by the retention of such property by the

debtor subject to such interests, claims, or liens, or (b) by a sale free of such interests, claims, or liens at not less than a fair upset price and the transfer of such interests, claims, or liens to the proceeds of such sale; or (c) by appraisal and payment either in cash of the value either of such interests, claims, or liens, or, at the objecting creditors' election, of the securities allotted to such interests, claims, or liens under the plan, if any shall be so allotted; or (d) by such method as will in the opinion of the judge, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection; * * * (9) shall provide adequate means for the execution of the plan, which may include the transfer of all or any part of the property of the debtor to another corporation or to other corporations, or the consolidation of the properties of the debtor with those of another corporation, or the merger or consolidation of the debtor into or with another corporation or corporations, or the retention of the property by the debtor, the distribution of assets among creditors or any class thereof, the satisfaction or modification of liens, indentures, or other similar instruments, the curing or waiver of defaults, extension of maturity dates of outstanding securities, the change in interest rates and other terms of such securities, the amendment of the charter of the debtor, and the issuance of securities of either the debtor or any such corporation or corporations, for cash, or in exchange for existing securities, or in satisfaction of claims or rights, or for other appropriate purposes."

Subsection (e):

"(1) A plan of reorganization shall not be confirmed until it has been accepted in writing, whether before or after the filing of the petition or answer under this section, and such acceptance shall have been filed in the proceeding by or on behalf of creditors holding two thirds in amount of the claims of each class whose claims have been allowed and would be affected by the plan and by or on behalf of stockholders of the debtor holding a majority of the stock of each class: *Provided, however,* that such acceptance shall not be requi-

site to the confirmation of the plan by any creditor or class of creditors (a) whose claims are not affected by the plan, or (b) if the plan makes provision for the payment of their claims in cash in full, or (c) if provision is made in the plan for the protection of the interests, claims, or liens of such creditor or class of creditors in the manner provided in subdivision (b), clause (5), of this section: *And provided further*, that such acceptance shall not be requisite to the confirmation of the plan by any stockholder or class of stockholders (1) if the judge shall have determined either that the debtor is insolvent, or that the interests of such stockholder or stockholders will not be affected by the plan, or (2) if provision is made in the plan for the protection of the interests of such stockholder or class of stockholders in the manner provided in subdivision (b), clause (4), of this section."

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No. 271

IN THE MATTER OF THE

620 CHURCH STREET BUILDING CORPORATION, A CORPORATION, DEBTOR UNDER SECTION 77B OF THE BANKRUPTCY ACT.

620 CHURCH STREET BUILDING CORPORATION, ET AL.,

Petitioners,

vs.

WARNER G. BAIRD, ET AL.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

Petition for Rehearing.

THEODORE E. REIN,
ISAAC M. MILLS,
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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

Petition for Rehearing.

To the Honorable Justices of the Supreme Court of the United States:

Comes now Emil Rosenthal and B. K. Goodman, petitioners for certiorari, by their counsel, and present this, their petition for re-hearing, and in support thereof respectfully show:

I.

Introductory Statement.

This case deals with the right of a District Court to confirm a plan of reorganization without the consent of junior lienors which deprives them of their liens, their right to a public sale, their right to bid and their right of redemption under the Illinois Statutes, all without compensation.

The 620 Church Street Building Corporation (herein referred to as Debtor) filed its voluntary petition for reorganization under Section 77B of the Bankruptcy Act. Its principal property, consisting of a building constructed on leased ground, is subject to three trust deeds executed prior to the enactment of Section 77B and securing:

a.	First mortgage bonds	$445,500
b.	Second mortgage notes	40,250
c.	Third mortgage notes	27,000

The plan approved by the District Court provides that the property of the Debtor shall be conveyed to the 636 Church Street Building Corporation, a separate and independent corporation, in consideration of stocks and bonds to be divided solely among the holders of the first mortgage bonds of the Debtor.

II.

Jurisdiction.

The Court of Appeals for the Seventh Circuit, denied petitioners leave to appeal from the order confirming the plan. This Court allowed certiorari. After a hearing, the

Court rendered its opinion on November 9th, 1936, to the effect that the Court of Appeals did not abuse its discretion in declining to allow the appeal.

III.

Reasons for Petition for Rehearing.

The opinion of this Court is based on the assumption that the District Court found as a fact that all the rights of the petitioners are of no value. This Court held that petitioners, being bound by the finding of the District Court, could not raise the constitutional question, having no value to protect.

The fact is that the District Court did not consider all the rights of petitioners and made absolutely no finding as to the most important of them.

The District Court found that petitioners' claims on their notes are of no value but made no finding as to the value of the substantive property rights of petitioners under their mortgages and the Statutes of Illinois, particularly their right to redeem the property of the Debtor.

Had the District Court fully considered petitioners' rights under their mortgages and under the Illinois Statutes, it would not have entered the order of confirmation in this case which, unless set aside by this Court, will have a disastrous effect on the security of all real estate mortgages and introduce a new and dangerous doctrine in the law of mortgages—a doctrine which will upset long established principles of law which have given stability to mortgage securities for many generations—a doctrine which will not appreciably facilitate proceedings under Section 77B—a doctrine which asserts that a mortgagor, by filing a peti-

tion in bankruptcy, may change the terms of a mortgage and destroy vested rights created thereby and by the statutes existing at the time the mortgage was executed.

Petitioners earnestly beg this Court to consider the grave consequences of its decision not only out of regard for the rights of petitioners but in view of its effect on the law of mortgages.

To demonstrate that the District Court did not make the finding of fact which this Court assumed and on the binding effect of which this Court based its opinion, petitioners desire to clearly point out the errors made by the District Court, namely:

A. The District Court erred in viewing the rights of the petitioners as being limited solely to a claim on the notes held by them. It overlooked their vested substantive rights in specific property arising out of and existing by virtue of the trust deeds securing the notes, and the statutes of the State of Illinois.

B. Granting that the District Court did not overlook the property rights of petitioners under their mortgages and the Illinois Statutes, then it erred in drawing from the testimony as to, and its finding of, the fair market value of the property of the Debtor, the erroneous inference that the vested property rights of petitioners are of no value.

C. The District Court erred in not ascertaining the value of the security to petitioners' notes by the methods set forth in Section 57 (h) of the Bankruptcy Act.

D. The District Court erred in confirming a plan which provided for the conveyance of the Debtor's property for a consideration not measurable in money and thereby depriving petitioners of their vested substantive rights in the property contrary to the Fifth Amendment.

IV.

ARGUMENT.

A. The District Court erred in viewing the rights of petitioners as being limited solely to a claim on the notes held by them. It overlooked their vested substantive rights in specific property arising out of and existing by virtue of the mortgages securing the notes, and the statutes of the State of Illinois.

The District Court placed the notes of the petitioners in classes 3 and 4 (R. 13), using the following language:

> "Class 3: Those claims allowed in these proceedings against 620 Church Street Building Corporation or its property, with respect to the notes secured by trust deed dated July 13, 1928, from Carlson Annex Building Corporation to B. K. Goodman, as trustee."
>
> "Class 4: Those claims allowed in these proceedings against 620 Church Street Building Corporation or its property, with respect to the note secured by trust deed dated June 3, 1931, from 620 Church Street Building Corporation to W. Kahn, as trustee."

The express language used refers to claims on the notes. The remaining words are descriptive of the notes and identify them.

Paragraph 12 of the order of confirmation (R. 15) covers the so-called appraisal of the above claims. The language, so far as applicable, is as follows:

> "That based on the above mentioned evidence and testimony *concerning the value of the Carlson Build-*

ing Annex, the Court has appraised and does hereby appraise all claims allowed in Classes 3 and 4 to be of no value * * *"

Here, too, the reference is definitely to the claims on the notes.

It is hardly necessary to point out to this Court that when notes are issued and secured by a mortgage on real estate, various rights come into existence. The notes evidence a personal obligation of the maker to pay the principal and interest at the time and in the manner specified in the notes. These obligations constitute claims of the holders of the notes to receive money from the maker, and may be discharged in bankruptcy. At the same time there come into being, property rights by virtue of the execution of the mortgage securing the notes and by virtue of the statutes of the state wherein the property described in the mortgage is located. These constitute substantive rights in specific property and are protected by the Fifth Amendment. In law, the claims on the notes and the property rights under the mortgage and statutes are entirely separate and distinct. These separations exist not only in law, they are frequent in fact. Whenever the mortgagor conveys its property and the grantee does not assume the payment of the debt, a separation occurs. The debt remains the obligation of the mortgagor. The rights in the property created by the mortgage and statutes follow the property into the hands of the grantee.

If the District Court intended to find the value only of the notes, from the standpoint of their immediate collectibility, its finding of no value based on the market value of the property of the Debtor and the amount of the first mortgage thereon is entirely correct. When, as in this case, the principal property of the maker is subject to several liens, it follows that the claims based on the

notes secured by a junior lien may readily be valued by finding the value of the property and deducting therefrom the amount due on the notes secured by the prior lien.

When, however, the District Judge confirmed the plan on the basis that the notes of petitioners were of no value, he overlooked entirely the rights of petitioners under their mortgages and the Statutes of Illinois. Let us look at those rights.

Petitioners, just as the Bank in the *Radford* case, possess certain rights by virtue of the junior mortgages and the Illinois statutes, namely:

1. The right to retain their lien on the property described in the mortgages until the lien is paid or until the lien is terminated, as provided by law, by a public sale of the property.
2. The right to bid at such sale.
3. The right to redeem from such sale within one year from the date of the sale by paying to the purchaser the amount bid.

Let us consider for a moment the most important and most valuable right of petitioners, namely, the right of redemption. Under the laws of Illinois this right of redemption continues for twelve to fifteen months after the sale of the property. It constitutes an option to acquire the property during this period at the price bid at the sale with interest. What gives great value to this right is the fact that the redemption price is not the market value of the property, not the amount of the prior liens, but the amount bid at the sale which frequently is much less. This right is the exact equivalent of the right to receive all the increases in the value of the property over

the bid price which may occur during the period of redemption.

Assuming that the price bid for the property of the Debtor at the sale is its market value as found by the District Court, namely, $245,025. On the date of the sale the exercise of the right to redeem would not yield a profit. But if real estate values increase during the twelve or fifteen months of the right of redemption, the option to acquire the property may be of great value.

This Court will take judicial notice that this country is emerging from one of the severest depressions ever experienced; that the trend of values is now definitely upward and that an option for twelve to fifteen months to acquire property at a fixed price may be very valuable. If values do not increase, the option need not be exercised. However, if, as seems likely, the value of the property increases to an amount in excess of the bid price, whatever it may be, whether due to increased industrial activity, reduction in interest rates or some form of inflation, petitioners may be able to realize a substantial sum by exercising their option.

The District Court entirely overlooked these rights. There is nothing in the order of confirmation referring to them, and the language used by the District Court shows that it did not give to these rights even the remotest consideration. It made absolutely no finding as to their value. It did not value the right to bid at the sale of the property of the Debtor. It did not value the right to redeem the property from the sale. It did not value the possible increases in the value of the property which may occur during the period of redemption. This is clearly and fully shown by the order of confirmation of the District Court, Class 3 and Class 4, of claims (R. 13) and paragraphs 11 and 12 (R. 15).

No public sale was had, hence there could be no opportunity to bid and no beginning or ending of the year in which to redeem, and of course, no bid price at which the redemption could be made. How could such rights be valued, depending as they do on future events incapable of ascertainment until they occur? There is no standard by which to measure their value. Merely to state the rights shows that they are valuable.

B. The District Court erred in drawing, from the testimony as to, and its finding of, the fair market value of the property of the debtor, the erroneous inference that the vested property rights of petitioners are of no value.

Petitioners agree that they are bound by the findings of fact made by the District Judge. However, they are not bound by any erroneous inference from such findings even though such inference be couched in the language of a finding of fact.

Paragraph 11 of the order of confirmation (R. 15) contains the following finding of fact:

> "That the court having heard evidence and testimony on the value of the property of the Debtor finds: * * * that the Carlson Building Annex has a fair market value of $245,025, and that there is no equity over and above the $445,500, principal amount of Carlson Annex Bonds. * * *"

The above is a finding of fact and petitioners are bound by it. From this finding, the District Court drew an inference, couched as a finding of fact, which is a mere conclusion of the Court and which petitioners urge is not binding on the petitioners unless it follows logically from the previous finding. Such an inference is subject to re-

view by this Court as is any conclusion of law. The inference or conclusion is found in paragraph 12 of the order of confirmation (R. 15) and reads as follows:

> "That based on the above mentioned evidence and testimony *concerning the value of the Carlson Building Annex*, the court has appraised and does hereby appraise all claims allowed in Classes 3 and 4 to be of no value." (italics ours.)

Assuming for the purpose of the argument on this point that the word "claims," as used in the above quotation, includes the substantive rights in specific property which petitioners have by virtue of their mortgages and the statutes of Illinois, then it is clear that the finding is a mere conclusion and does not follow from any testimony as to the value of the property of the Debtor. Manifestly, evidence as to the present market value of the building and leasehold cannot be the basis for a conclusion as to the value of petitioners' right to redeem or option to acquire the property for a period of twelve months after a sale of the property at the price bid therefor.

The record is complete on this point and contains everything necessary to enable this Court to determine whether the inference follows from the finding of fact or whether it is merely the erroneous conclusion of the District Judge.

It is respectfully urged that whatever value there may be in the vested rights of petitioners heretofore specifically enumerated and which this Court appears to concede in its opinion that petitioners possess, it cannot be determined by looking solely at the evidence as to the present market value of the property covered by the mortgages. Obviously, the property may have a market value less than the first mortgage. Still, the right to redeem,

or option to acquire the property during a period of one year, not at its market value or at the amount due on the first mortgage, but at the amount bid at the sale, may be of great value. For example—suppose the property have a market value of $250,000, the first mortgage being $450,000, and a sale is held and the price bid is $200,000. An option to purchase at the bid price for one year is worth at least $50,000 based on present values. When conditions are improving and the tendency is perceptibly upward, such an option may become of great value. In its November, 1936 bulletin, the Federal Reserve System states that the index of industrial production has risen from 64% in 1932 to 108% in the third quarter of 1936.

A good illustration of the value of an option may be taken from the stock market. From June 1932 to June 1933, American Can Company stock rose from 30 to 95, American Telephone & Telegraph Company from 77 to 132 and Standard Oil of New Jersey from 19 to 38. An option on 1000 shares of each of these stocks at the market in June 1932 would in June 1933 have a value of $139,000.

If the conclusion drawn by the District Court is not logical, it is not binding on petitioners.

C. The District Court erred in not ascertaining the value of the security to petitioners' notes by the methods set forth in Section 57 (h) of the Bankruptcy Act.

The only explanation for the failure of the District Court to follow the plain directions of subdivision (b) (5) of Section 77B of the Bankruptcy Act in respect of the valuation of the security behind the notes of petitioners is that the District Court overlooked the fact that petitioners had any rights under the mortgages securing the notes. The language used by Congress is unmistakable. Towards the end of subdivision (b) (5) of Section 77B appears the following:

> "In the case of secured claims entitled to the provisions of clause (5) of this subdivision (b), the value of the security shall be determined in the manner provided in Section 57, clause (h) of this Act, and if the amount of such value shall be less than the amount of the claim, the excess may be classified as an unsecured claim."

Section 57 (h) of the Bankruptcy Act reads as follows:

> "The value of securities held by secured creditors shall be determined by converting the same into money according to *the terms of the agreement pursuant to which such securities were delivered to such creditors* or by such creditors and the trustee, by agreement, arbitration, compromise, or litigation, as the court may direct, and the amount of such value shall be credited upon such claims, and a dividend shall be paid only on the unpaid balance." (italics ours.)

Remington on Bankruptcy, Volume 7, Fourth Edition, Page 326, Paragraph 3153.32, discussing the treatment pro-

vided by Section 77B to be accorded non-assenting secured creditors, says:

> "The statute requires that their interests be adequately protected in one of the following ways: * * * (3) by appraisal and payment in cash of either the value of the interest or of the value of the securities allotted to such interest under the plan, this last to be at the option of the objecting creditors. *Any appraisal is to be worked out as provided for in Section 57 (h) of the Bankruptcy Act.*" (italics ours.)

A secured creditor is defined in Clause 23 of Section 1 of the Bankruptcy Act as a creditor who has security for his debt upon the property of the bankrupt. It is well established that the holder of a note secured by a mortgage on real property is within the class of secured creditors contemplated by Section 57 (h) of the Bankruptcy Act.

It is submitted that the record clearly shows that the District Court did not follow the law.

D. The District Court erred in confirming a plan which provided for a conveyance of debtor's property for a consideration not measurable in money and thereby depriving petitioners of their vested substantive rights in the property contrary to the Fifth Amendment.

Prior to the passage of the amendment to the Bankruptcy Act, petitioners became the owners of the substantive rights on specific property, heretofore enumerated, by virtue of the execution of their mortgages and of the Statutes of Illinois. All of these rights were wiped out without compensation by the plan of reorganization approved by the District Court in this case, and bestowed on a private corporation for private use. It is hard to conceive a more thorough deprivation of property.

The plan directed the Debtor to convey its property free of all claims to the 636 Church Street Building Corporation for a part of its stock and bond issues to be distributed among the holders of the first mortgage bonds of Debtor. In effect, the plan and the order of the District Court took the rights in the property which petitioners had and gave them to others without compensation.

There is no provision in the Bankruptcy Act, as amended, for such action. If there were, it would be clearly in violation of the Fifth Amendment.

If the District Court assumed that clause (c) of subdivision (b) (5) of Section 77B of the Bankruptcy Act contains the necessary authority, it overlooked the provision in subdivision (b) (5) providing that in case of secured claims, the value of the security shall be ascertained as provided in Section 57 (h) of the Bankruptcy Act. Under this section, petitioners would have been entitled to have a judicial sale with the accompanying right to bid thereat and to redeem.

Suppose, that the District Court had recognized that petitioners had the right to redeem and had placed a value upon it of, say, $10,000. Is there any provision in the law of the land which would permit any court to compel petitioners to surrender their right at that price to a private corporation for private use?

V.

General.

At the hearing on the petition for certiorari counsel for petitioner was asked by this Court if no plan of reorganization could be consummated without the consent of junior lienors. Inadvertently counsel stated that it could not, but what counsel intended to say was that no plan could be effectuated unless it preserved the rights of the junior lienors under the mortgages.

Petitioners concede that the plan of reorganization adopted in this case would be proper if it provided for a public sale of the property of the Debtor so that the junior lienors would be afforded the opportunity of bidding at the sale and of redeeming from the sale within one year from its date by paying the purchase price bid at the sale, with interest, in accordance with the Statutes of Illinois.

It is difficult to see why such a course was not adopted by the District Court. The owners of the first mortgage bonds would have had the opportunity of bidding for the property at such a public sale and if the same were acquired on their behalf they could, under the plan of reorganization, apply the first mortgage bonds to the purchase price. If the price bid were less than the amount of the first mortgage bonds, no cash outlay would be involved. If more, the excess would be applicable to the junior liens. Of course, the purchaser would acquire the property subject to the right of redemption of the junior lienors. At the expiration of the redemption period, if no redemption were made, the property would vest absolutely in the purchaser. If the property were acquired on behalf of the first mortgage bondholders and they desired to transfer it to the 636 Church Street Building Corpora-

tion for a consideration to be paid in stocks and bonds, they could do so with the same effect as is attempted to be done by the order of the District Court in this case.

Petitioners submit that this was the only course which the District Judge was authorized to pursue under the provisions of Section 77B, and that such a course is free from any constitutional objections on the part of junior lienors.

Petitioners recognize that in some instances a consummation of the plan of reorganization may be somewhat retarded by the requirement of the consent of junior lienors. However, if the junior lienors are unreasonable in their demands, it lies in the power of the District Court to confirm a plan without their consent by ordering a public sale of the property of the debtor, subject to the rights of the junior lienors, as heretofore pointed out. The plan of reorganization would be in no way affected except that for a period of one year after the date of sale the right of redemption would exist.

On the other hand such a requirement would eliminate any fear on the part of junior lienors of losing their rights and act as a check on unreasonable demands on the part of the holders of the first mortgage. This would be a wholesome and salutary condition and tend to make each party in interest adopt a fair attitude towards the others.

This court ought not to be influenced by the apparent great disparity in the market value of the property of the debtor as found by the District Judge and the amount of the first mortgage bonds. This is but an accident of this case. If the principle is applicable where the difference is large, it should govern in cases where the difference is slight and even in cases where the market value of the property is found by a court to be in excess of the

first mortgage bonds so that a surplus is applicable to the holders of the junior lien.

The Court will bear in mind that opinions as to the market value of property during a depression differ greatly. Witnesses are but human and their pessimism or optimism or unconscious bias frequently influence their testimony.

The so-called plan of reorganization in this case constitutes simply a transfer of the property of the Debtor to a stranger to the proceedings for a consideration distributed to the holders of the first mortgage bonds. In effect it is simply a foreclosure of the first mortgage lien, with the advantage to the holders of the first mortgage that it deprives junior lienholders of their right to a public sale, the opportunity to bid at the sale and their right to redeem. The unfairness of the plan becomes manifest when one visualizes the result in the light of the upward trend of the market and the possibility that during the period of redemption allowed by the Statutes of Illinois the market value of the property may greatly increase. These advantages conferred by law on the junior lienors were taken from them and conferred on the holders of the first mortgage bonds and on the 636 Church Street Building Corporation.

Petitioners respectfully further urge that once it is admitted that property has been taken without due process, there is never any question of the value of the property. The Fifth Amendment directs that no one shall be deprived of life, liberty or property without due process of law. The words are without limitation.

It would be a strange doctrine that would prevent one who has been deprived of his home or farm by a statute contrary to the Fifth Amendment from questioning the

constitutionality of the statute because his home was a hovel and of no value in the opinion of real estate men, or that his farm consisted of swamp land which could not yield a crop in excess of the value of the labor put upon it.

Petitioners are aware of the doctrine exemplified by the authorities cited in the opinion of this Court, that one may not question the constitutionality of a law which does not affect him directly. Of course, one may not question a law which deprives others of property. In the instant case, however, petitioners have been deprived of their vested, substantive rights in specific property and are, therefore, clearly within the class who may question the constitutionality of the law or of the judicial act under which such deprivation has been effected.

VI.

Public Importance of Issues.

Effect on Mortgages:

It took many years to develop an investment market for real estate mortgages. At first, property holders were reluctant to place mortgages on their property and much time elapsed before even first mortgages came into favor. Knowledge of the advantages in the purchase of a home or other property, with a small initial payment, spread slowly. Dealings in second mortgages were regarded with still less favor. Prejudice in this field, too, slowly decreased and in recent years it was generally recognized that the increase in credit made possible by the issuance of notes and bonds secured by first and junior mortgages had a stimulating effect on industry. Particularly is this true in the building industry.

Subsidiary financing (that is, the money provided for an enterprise to supplement that provided through the sale of first mortgage securities) has been growing in importance. Prior to the depression, in 1929, it had become a recognized factor in finance and was regarded as a useful and necessary source for the supply of part of the capital required in the financing of industrial enterprises, the erection of buildings and the sale of homes. The money thus furnished contributed to the general prosperity.

If unhampered, junior lien securities will become increasingly important in financing new industries, the expansion of existing plants, the replacement of obsolete and worn-out machinery and particularly the revival of the building industry, all of which must come if this country is to recover completely from the depression.

As dealings in mortgage securities increased, the rights of mortgagees became well established. Among the rights possessed by mortgagees which made mortgages desirable investments are the following:

(1) The right to retain the lien of the mortgage, first or junior, until the debt is paid or until the lien is terminated by a judicial public sale in accordance with the Statutes of the state in which the property is located.

(2) The right to bid at the sale.

(3) In the case of a junior lien, the right to redeem the property from the purchaser at the sale if the purchaser should be the prior lienor or a stranger.

It is universally believed that the above rights are protected by the Fifth Amendment to the Constitution and that no mortgagee can be deprived of any of these rights by any act of the mortgagor or because of any financial diffi-

culties the mortgagor might encounter. Millions of dollars have been invested in mortgage securities, both first and junior, in reliance on this belief.

The right of redemption, developed originally to prevent the wiping out of the equity as the result of a temporary collapse of values due to a temporary financial disaster, is greatly valued by the junior lienor as it affords him the same protection.

Under the laws of Illinois this right continues for one year or fifteen months, and the price at which redemption can be made is fixed by statute at the price bid at the sale. These rights protect the junior lienholder from total loss should he be unable to raise sufficient money on short notice.

The order of the District Court in this case is founded on the assumption that these rights may be wiped out in a proceeding under Section 77B of the Bankruptcy Act. Under such assumptions the District Court may, in any such proceeding, arrive at the value of the property covered by mortgages by receiving the testimony of men engaged in the real estate business as to its then market value, and when in such case the court finds that the then market value of the property is less than the prior charges thereon, the court may wipe out all liens subsequent to such prior charges and all rights accruing under them. Thus, it may happen even in the case of a first mortgage that the court may find that the prior charges consisting of the expenses of the proceedings, taxes, etc., are greater in amount than the then market value of the property and as a result without giving any of the mortgagees, first or junior, an opportunity to hold a public sale of the property subject to their mortgages, or to bid at such sale, or to redeem therefrom, the court may order such property conveyed to a stranger upon its paying the amount of the prior charges.

If a District Court has such power in a proceeding under Section 77B, it would logically follow that it would also have the authority, in case it found that the property was worth more than the prior charges, to direct the conveyance of the property upon the payment of the excess to the lienholders.

Apparently in all such instances it would be of no effect for the holders of the senior or junior liens to plead that in their opinion the property was worth more than the value placed upon it by the Court, and that they desired to avail themselves of the right to acquire the property at an amount equal to, or greater than, the value found by the Court, or that such lienors desired the property sold at a judicial public sale and desired the right to bid thereat, and if unsuccessful, to redeem within the statutory period.

This is a new and dangerous doctrine, heretofore unheard of in the law of mortgages. It implies a power that ought not to be lodged in the District Court. It is inimical to that freedom of contract which is so necessary to industrial prosperity.

Nor can it be said that such power in the hands of the District Court will facilitate the consummation of plans of reorganization in cases where the necessary consents cannot be obtained. In all proper cases, property subject to non-consenting lienors may be ordered sold at public auction subject to the right of the lienors to bid and to redeem under the Illinois Statutes. The delay due to a public sale and the inconvenience of having the property subject to redemption are trifling in comparison to the confusion created by the introduction of a new doctrine in the law of mortgages.

Effect on 77 B Proceedings:

Congress passed the amendment to the Bankruptcy Act because it believed that a speedier and less expensive proceeding than the Equity Receivership would facilitate recovery from the depression and be permanently useful. It would appear, therefore, that proceedings thereunder should be encouraged. General industry is benefited whenever corporations or properties in financial difficulties are relieved, taken out of the hands of the courts and given their proper place in industry under private management.

Obviously the holders of equities will be reluctant to file proceedings if by filing the same they run the risk of losing their equity because of a determination by the District Judge, based on opinion evidence, that the present market value of the property involved is less than the amount of the first mortgage. It will be impossible to procure the cooperation of junior lienholders if by coming into the proceedings they risk the loss of vested rights long regarded as necessary for the protection of their investment.

A majority of the proceedings under the amendment are filed voluntarily. In many instances the debtors have committed no act of bankruptcy and involuntary proceedings could not be filed under the law. Hence, it is clear that if the order of confirmation entered in this case is upheld, the number of proceedings filed under the amendment will be greatly reduced.

VII.

Conclusion.

It is respectfully urged that out of regard for the important issues involved affecting, not only the parties to this case but the large number of public and private institutions and individual investors in real estate mortgage securities, this petition for rehearing be granted; that upon further consideration, the order of this Court of November 9th, 1936, be vacated or modified, and that the parties be given another opportunity to argue and present this cause; and that on final hearing the order of the Circuit Court of Appeals for the Seventh Circuit denying petitioners leave to appeal from the order of the District Court be reversed.

Respectfully submitted,

THEODORE E. REIN,
ISAAC M. MILLS,
Counsel for Petitioners.

Certificate of Counsel.

We, Theodore E. Rein and Isaac M. Mills, counsel for the above named petitioners, Emil Rosenthal and B. K. Goodman, do hereby certify that the foregoing petition for rehearing of this cause is presented in good faith and not for delay.

THEODORE E. REIN,
ISAAC M. MILLS,
Counsel for Petitioners.

SUPREME COURT OF THE UNITED STATES.

No. 271.—October Term, 1936.

In the Matter of 620 Church Street Building Corporation, et al., Petitioners. } On Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

[November 9, 1936.]

Mr. Chief Justice Hughes delivered the opinion of the Court.

In this proceeding under Section 77 B of the Bankruptcy Act, the District Court confirmed a plan of reorganization. Petitioners asked the Circuit Court of Appeals to allow an appeal upon the ground that the plan was unfair and inequitable and deprived them of their property without due process of law in violation of the Fifth Amendment. Bankruptcy Act, Sections 24 (b), 77 B (k); *Meyer* v. *Kenmore Hotel Co.*, 297 U. S. 160, 165, 166. Leave to appeal was denied. In view of an asserted conflict with the decision of this Court in *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, and with that of the Circuit Court of Appeals of the Sixth Circuit in *Tennessee Publishing Company* v. *American National Bank*, 81 F. (2d) 463, (*ante*, p. —), this Court granted certiorari. — U. S. —.

Although the Circuit Court of Appeals declined jurisdiction, its action may properly be reviewed upon a writ of certiorari under the general power conferred by Judicial Code, Section 262. 28 U. S. C. 377. That provision contemplates the employment of this writ in instances not covered by Section 240 of the Judicial Code (28 U. S. C. 347), and affords ample authority for using the writ as an auxiliary process and as a means "of giving full force and effect to existing appellate authority and of furthering justice in other kindred ways". *United States* v. *Beatty*, 232 U. S. 463, 467; *American Construction Co.* v. *Jacksonville Railway Co.*, 148 U. S. 372, 379, 380; *In re Chetwood*, 165 U. S. 443, 461, 462; *Magnum Company* v. *Coty*, 262 U. S. 159, 162.

The record presents the petition for appeal and the order confirming the plan of reorganization. It appears that the principal

property of the debtor, the 620 Church Street Building Corporation, consists of certain leaseholds and improvements known as the Carlson Building Annex. The allowed claims include first mortgage bonds of $445,500 upon which interest is due from January, 1931, second mortgage notes for $40,250, with interest from December, 1929, and a third mortgage note for $27,000, with interest from December, 1931. Petitioners are the debtor, the holders of the second and third mortgages, and stockholders.

The order of confirmation sets forth the findings of the District Court that the property in question has a fair market value of $245,025 and that there is no equity over and above the $445,500 of the first mortgage bonds; that the debtor is insolvent; that the claims of the junior lienors, the holders of the second and third mortgages, are of no value and hence that no securities or cash should be distributed under the plan in respect to their claims; that stockholders are not entitled to participate in the plan; and that the plan is "fair, equitable, and feasible and does not discriminate unfairly in favor of any class or classes of creditors or stockholders".

The evidence before the District Court is not presented by the record. And as the Court of Appeals, if the appeal had been allowed, could have revised the ruling of the court below only in matter of law, it necessarily follows—and was conceded at the bar—that petitioners are bound by the findings of fact. Petitioners insist that their consent to the plan of reorganization was necessary or that their claims should have been accorded "adequate protection". But the adequate protection to which the statute refers is "for the realization of the value of the interests, claims or liens" affected. Here the controlling finding is not only that there was no equity in the property above the first mortgage but that petitioners' claims were appraised by the court as having "no value". There was no value to be protected. This finding embraces whatever interests petitioners may have as junior lienors under the Illinois law and, in the same aspect, the constitutional argument is unavailing as petitioners have not shown injury. *Southern Railway Co.* v. *King*, 217 U. S. 524, 534; *Standard Stock Food Co.* v. *Wright*, 225 U. S. 540, 550; *Plymouth Coal Co.* v. *Pennsylvania*, 232 U. S. 531, 544, 545; *Heald* v. *District of Columbia*, 259 U. S. 114, 123.

The Circuit Court of Appeals did not abuse its discretion in declining to allow an appeal.

Affirmed.